No. 04-1208 MAR 7 - 2005

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In The Supreme Court of the United States

ANN MOSTOLLER, TRUSTEE,

Petitioner,

v.

CW CAPITAL, LLC,

Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

---

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED FOR REVIEW

Do principles of estoppel and waiver apply to Respondent CW Capital, LLC, a private lender, in the context of a HUD-insured loan so as to preclude a grant of summary judgment to CW Capital?

LIST OF ALL PARTIES TO THE PROCEEDING IN THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT AND CORPORATE DISCLOSURE STATEMENT

In addition to the parties named in the caption, West Pointe Properties, LP, is the real party in interest. West Pointe has no parent corporation, and no publicly held company owns any stock in West Pointe.

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OPINIONS BELOW

The Memorandum and Order of the District Court at No. 3:02-CV-291 granting Defendant-Respondent CW Capital's Motion for Partial Summary Judgment as to Plaintiff-Petitioner's claim for damages is set forth in the Appendix at A-32. The Memorandum Opinion of the District Court granting Defendants' Motions for Summary Judgment and dismissing the action is set forth in the Appendix at A-15. The Judgment Order of the District Court granting Defendants' Motions for Summary Judgment and dismissing the action is set forth in the Appendix at A-13. The Opinion of the United States Court of Appeals for the Sixth Circuit, *Mostoller v. CW Capital, LLC*, 2004 WL 2792508 (6th Cir. 2004) (unpublished), affirming the judgment of the district court is set forth in the Appendix at A-1.

JURISDICTION

This matter was filed as an adversary proceeding in the United States Bankruptcy Court for the Eastern District of Tennessee. The Bankruptcy Court had jurisdiction pursuant to 28 U.S.C. §§ 1334(a) and 157(a) and (b). The United States District Court subsequently took jurisdiction pursuant to 28 U.S.C. § 157(d). The judgment of the United States Court of Appeals for the Sixth Circuit was filed on December 6, 2004. The jurisdiction of the Court is invoked pursuant to 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

This matter involves a contract for a loan federally insured by the Department of Housing and Urban Development under the National Housing Act Amendments of 1938, 12 U.S.C. §§ 1701 et seq. However, no particular provision of the Act is at issue.

Fed. R. Civ. P. 56 provides in pertinent part as follows:

> **(a) For Claimant.** A party seeking to recover upon a claim, counterclaim, or cross-claim or to obtain a declaratory judgment may, at any time after the expiration of 20 days from the commencement of the action or after service of a motion for summary judgment by the adverse party, move with or without supporting affidavits for a summary judgment in the party's favor upon all or any part thereof.
>
> **(b) For Defending Party.** A party against whom a claim, counterclaim, or cross-claim is asserted or a declaratory judgment is sought may, at any time, move with or without supporting affidavits for a summary judgment in the party's favor as to all or any part thereof.
>
> **(c) Motion and Proceedings Thereon.** The motion shall be served at least 10 days

before the time fixed for the hearing. The adverse party prior to the day of hearing may serve opposing affidavits. The judgment sought shall be rendered forthwith if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law. A summary judgment, interlocutory in character, may be rendered on the issue of liability alone although there is a genuine issue as to the amount of damages.

STATEMENT OF THE CASE

In light of the question presented and the reliance on factual errors by the lower courts in their opinions, it is necessary to set out the facts in some detail so as to properly understand the importance of the legal question presented and the injustice done to the Petitioner in this case.

This case involves a contract dispute between two private parties in connection with a loan insured by the Department of Housing and Urban Development. West Pointe Properties claims that Continental Wingate Associates breached the contract by its improper declaration of default under a building loan agreement between the two parties.

On May 26, 1999 West Pointe Properties, LP ("West Pointe"), filed a voluntary Chapter 11 petition (business reorganization) in the Bankruptcy Court for the Eastern District of Tennessee at Knoxville. On November 4, 1999, this adversary proceeding was filed by West Pointe against Appellee Continental Wingate Associates, Inc. (now CW Capital, LLC, and hereinafter "CW"), for wrongfully terminating a construction loan for Phase I of a manufactured home community ("West Pointe Community") to be located in Knoxville, Tennessee, and also against the United States of America, Department of Housing and Urban Development ("HUD"), for not reinstating the loan after it had been assigned to HUD for collection. The wrongful termination of the lending relationship by CW caused a loss of West Pointe's development of both contemplated phases (Phase I and Phase II) of the West Pointe Community. In summary, the case against CW was for breach of contract, also known as lender liability.

On December 9, 1999, West Pointe's bankruptcy case was converted to Chapter 7 (liquidation), and thereafter Ann Mostoller was appointed trustee and substituted as the named plaintiff for this suit. On June 6, 2002, the standing order of reference was removed, and the case was transferred to the District Court for the Eastern District of Tennessee, at Knoxville, for trial by jury.

On December 5, 2002, CW filed a motion for partial summary judgment as to West Pointe's Phase II damages claim. West Pointe had contended that when the first phase was lost, the net profits for Phase II of the

development were also lost as a consequence of the breach (i.e., consequential damages). On March 6, 2003, the district court entered an order granting CW's motion.

On January 14, 2003, the trustee filed a motion seeking to voluntarily dismiss HUD. HUD agreed to the motion, yet the District Court never ruled on this motion.

On February 24, 2003, CW filed a motion for summary judgment on all remaining issues. Even though the trustee and HUD had agreed that the claim against HUD was to be voluntarily dismissed, HUD joined in the motion. On July 18, 2003, the district court entered an order granting both motions, and the case was dismissed.

West Pointe's remedy against HUD for post-termination failure to reinstate the loan was relevant only if West Pointe failed to collect from CW. Since the trustee had sought long ago to dismiss HUD for this reason, the trustee only appealed the dismissal of its suit against CW. On December 6, 2004, the Sixth Circuit affirmed the judgment of the district court.

1. Background To The West Pointe Community

In 1989 Ronald Frye, a resident of Knoxville, Tennessee, began plans to develop 64 acres of land in Knox County, Tennessee, as a manufactured housing community to be called the "West Pointe Community." The community was to have large lots, paved roads with roll-curbing and guttering, professional landscaping with hundreds of trees, laundry facilities, a clubhouse, and a

swimming pool. In short, the development was to be a very attractive and upscale place for low- to median-income families to call home. As with many large developments of this sort, it made economic sense to develop the site not all at once, but in two phases. It is also common to undertake these developments in the form of real estate partnerships and development companies. By 1991, Mr. Frye directly owned, or owned and controlled entities that did own, all 64 acres for the proposed West Pointe project.

West Pointe was to make money by leasing lots to residents, sales of homes in the community to prospective residents, and from certain amenities on site, such as rental of storage units and coin-operated laundry fees. Phase I, situated on the first 33 acres, was to have 150 home sites, 14 storage units, a clubhouse, a swimming pool, and laundry facilities, and Phase II, to be situated on the remaining acres adjoining Phase I, was to have 200 home sites and 48 storage units.

2. The Construction Loan With CW

To build West Pointe Community, West Pointe obtained a construction loan in the amount of $2,222,900 with CW to finance Phase I, and that loan was closed August 7, 1996, in Knoxville, Tennessee. The loan was insured by HUD. The August 7, 1996 closing documents included many documents, including a construction Loan Agreement and an Extension Agreement. The construction Loan Agreement required construction to be completed by July 7, 1997, and if construction was not completed by that date, then CW in its discretion, could

terminate the loan. If CW elected not to terminate the loan, the Extension Agreement set forth the terms of continued construction.

To obtain the HUD insurance, CW signed and presented the business pro forma for the project to HUD. That pro forma at section H, line 5, shows that as of the date of the application (1/3/94), the West Pointe Community would generate $240,014 in annual net income for at least the life of the 40-year loan. HUD's independent analysis of the project confirmed annual net income to be $236,407, also for the 40-year loan.

3. West Pointe's Construction Contract With Hicks

To build the project, West Pointe contracted with J. Hicks Excavating, Inc. ("Hicks"). The Hicks construction contract ("Hicks Contract"), also executed August 7, 1996, was for actual costs of construction not to exceed $1,653,540 on which West Pointe purchased performance and payment bonds with USF&G. Although West Pointe's Loan Agreement with CW required construction to be finished by July 7, 1997, the Hicks Contract set a completion date of February 7, 1997. Due to extraordinary rain during construction, the Hicks Contract completion date was extended to May 5, 1997.

On May 5, 1997 construction was still incomplete, and so both West Pointe and CW requested that HUD extend the completion date under the Hicks Contract to September 30, 1997. The significance of an extension of time under the Hicks Contract to complete the project has to do with the liquidated damages clause at Article 2(c)

of that contract, in the penal sum of $769.12 per day in the event construction was not completed by May 5, 1997. The Hicks Contract stated that the liquidated damages money was to be used to pay West Pointe's loan interest, taxes, mortgage insurance premiums, liability insurance premiums, and construction and permanent loan extension fees. Also, it cannot be over-emphasized that Hicks had a performance bond in the amount of $1,653,540 with USF&G to complete the project in the event of a default by Hicks.

Unfortunately for Hicks and its surety, the joint request by West Pointe and CW for an extension of the Hicks Contract deadline to September 30, 1997 was denied by HUD directive dated July 9, 1997. The significance of that denial was the triggering of the assessment of liquidated damages against Hicks of $769.12 per day, retroactive to May 5, 1997, such that thereafter, all increased costs of construction for the delay in completion—to whenever that would be—would be paid by Hicks or its surety, USF&G. The good news for CW and West Pointe was that HUD's decision to deny an extension to the Hicks Contract meant that although construction was not on time, construction would continue at no additional cost to CW or West Pointe.

4. The Events Following July 7, 1997

In the event construction was not completed by July 7, 1997, Paragraph 9 of the Loan Agreement between West Pointe and CW granted the Lender (CW) the following discretion: "[T]he Lender, at its option, may terminate this agreement." On July 7, 1997, construction

was not complete, and CW did not terminate the loan. In so doing, the parties by definition operated under the Extension Agreement. Additionally, the parties followed the July 9, 1997, directive from HUD. The HUD letter, in pertinent part states:

> My staff has not observed a proper, concerted effort on the part of the general contractor to complete this job in a timely manner.
>
> Based on the above situation, the liquidated damages clause in the construction contract must be relied on as a source of funds for potential overruns in interest, taxes, mortgage insurance premiums, and property insurance.
>
> Under provisions of HUD Handbook 4435.1 REV-1, paragraph, 4-5C., I have authorized the transfer of funds from the construction account to cover these soft costs to an assumed revised completion date of September 30, 1997. A minimum estimated amount of $60,000.00 has been transferred from column J, Construction, to column G, Carrying Charges on form HUD-92451, Financial Record of Mortgage Loan Transaction. . . .
>
> This transfer is a minimum at this time to cover soft cost expenses. The actual amount of the reduction in the contract

sum for late completion of the project is the lesser of actual damages or $769.12 for each day of delay as set forth in Article 2 of the construction contract. This computation is reduced by any net operating income during the damage period.

Note that HUD does not blame West Pointe for the situation nor instruct CW to terminate the loan. The HUD directive also does not set a new date by which construction *must* be completed because a new date was not needed. Completion was literally insured, at no additional cost to CW, HUD, or West Pointe, due to the performance bond and the liquidated damages assessed Hicks.

5. Construction Loan Financing

Construction loan financing is quite different from traditional lending relationships. For example, for the first year of the loan, West Pointe did not, nor was it supposed to, make "payments," as in sending CW a monthly check as one might do on a home mortgage payment or car loan. Construction loan advances were effected by periodic instructions from West Pointe to CW to draw down on the loan. Likewise, the interest to cover the advances on the loan during construction (the "construction interest") was to be "paid" by these draw requests. As can be seen, timeliness of the submission of these draw requests was never material for CW because West Pointe was technically not making payments. West Pointe was just sending a piece of paper to CW so that it

could make the various ledger entries and pay itself from money at its disposal.

CW was paid the regular principal payments due for August and September 1997. For the construction interest due for those two months, West Pointe submitted Draw Request No. 11 on October 10, 1997 in the amount of $15,251. HUD approved this draw on the loan on October 20, 1997, and CW paid itself thereafter. For the October principal due November 1, 1997 (with a grace period until November 15, 1997), West Pointe sent its check in the correct amount, and said check was timely received by CW on Monday, November 17, 1997, which was the next business day. For the October interest and other soft costs due at the same time, and with the same grace period, West Pointe sent to CW Draw Request No. 12 along with the previously mentioned check for October principal, which CW likewise timely received on November 17, 1997. On either the same day or the next, CW processed and credited the loan accordingly. This is proven by the fact that on November 18, 1997, CW automatically generated a past-due reminder for this West Point Loan. The November 18, 1997 past-due reminder for the West Pointe loan showed that as of that time, there was no outstanding principal or interest due!

6. Termination Of The Loan December 10, 1997

CW does not know when it decided to default West Pointe. However, it was after November 20, 1997, because on that date CW wrote West Pointe demanding loan extension fees, which it would only do if the loan was not in default. As previously mentioned, loan

extension fees were not to be "paid" by West Pointe, but instead from the liquidated damages assessed Hicks.

By letter dated December 10, 1997, Gardener Hall, vice-president for CW, sent to West Pointe a letter declaring the loan terminated for basically three reasons, which were (1) failure to make the October interest payment, (2) abandoning the project, and (3) failure to complete construction by July 7, 1997. The letter enumerated five reasons, but two of those reasons were repetitious. Simultaneously, CW seized the $128,619 letters of credit and paid itself the entire amount—all over a purported $8,005.54 dispute. The trustee presented sufficient, if not compelling, facts in the record demonstrating that the stated CW reasons for default were false. The absurdity of terminating the West Pointe construction cannot be overemphasized. Due to the bond and the liquidated damages provision, continuing construction would have been at no additional cost to CW, West Pointe, or HUD. Instead, CW collected over $1 million of the taxpayers' money as loan insurance proceeds from HUD.

ARGUMENT

PRINCIPLES OF ESTOPPEL AND WAIVER APPLY TO RESPONDENT CW, A PRIVATE LENDER, SO AS TO PRECLUDE THE GRANT OF SUMMARY JUDGMENT TO CW.

This is a dispute between two private parties, West Pointe and CW. HUD is not a party to this proceeding. The Sixth Circuit opinion fails to understand the

significance of this fact, however, and renders a holding contrary to the law and in conflict with other circuits. The Sixth Circuit opinion affirming the grant of summary judgment to CW was based on its findings that the contract authorized CW to declare default if West Pointe failed to meet the construction deadline and that West Pointe failed to meet the deadline. The court refused to consider any other circumstances. Due to such determination, the court did not consider the remaining claims. The court's findings were based on numerous factual errors but also were based on misapplication of the applicable law, and, in rendering its opinion, the court has entered a decision in conflict with decisions in other circuits. Furthermore, the question presented raises an important issue that should be addressed by this Court to provide guidance to the lower courts, as well as to insure that justice is served in this case.

West Pointe's main contention in arguing that CW breached the loan agreement is that West Pointe's failure to complete the construction by the July 7, 1997 deadline was not a valid reason to terminate the loan on December 10, 1997, due to the admissions and conduct of CW following July 7, 1997. West Pointe specifically pointed to the following four facts which supported its position that the termination in December for the reasons asserted by CW was wrongful and in bad faith: (1) the directive from HUD; (2) the Extension Agreement; (2) waiver by CW; and (4) West Pointe's detrimental reliance (estoppel).

The Sixth Circuit summarily rejected West Pointe's claims based not only on factual errors but also on its legal conclusion that federal law governed the

interpretation of a HUD-backed loan and the rights and liabilities of the parties under such a loan and, therefore, that doctrines of waiver and estoppel cannot modify the terms of a HUD-insured loan, even if the facts supported their application. In support of these conclusions of law, the court relied primarily on *United States v. Victory Highway Village, Inc.*, 662 F.2d 488 (8th Cir. 1981). *Victory Highway Village*, however, involved a claim of estoppel and waiver against HUD, not the private lender, as is the case here. This is an important distinction not taken into account or even mentioned by the Sixth Circuit. In failing to address this fact and in rejecting West Pointe's claims of waiver and estoppel, the Sixth Circuit holding is in conflict with other circuits with regard both to its application of federal rather than state law and to its rejection of the claims of waiver and estoppel. As explained in *United States v. Kimbell Foods, Inc.*, 440 U.S. 715 (1979), whether federal law does or does not apply to West Pointe's cause of action against CW is by no means the end of the analysis.

> Controversies directly affecting the operations of federal programs, although governed by federal law, do not inevitably require resort to uniform federal rules. . . . Whether to adopt state law or to fashion a nationwide federal rule is a matter of judicial policy. . . .
>
> . . . [W]hen there is little need for a nationally uniform body of law, state law may be incorporated as the federal rule of decision. Apart from considerations of

> uniformity, we must also determine whether application of state law would frustrate specific objectives of the federal programs. . . . Finally, our choice-of-law inquiry must consider the extent to which application of a federal rule would disrupt commercial relationships predicated on state law.

Id. at 727-30 (citations omitted; footnotes omitted). In *Kimbell Foods*, deciding whether to apply federal law hinged upon safeguarding the federal treasury from defaulting debtors. *Id.* at 729. West Pointe's suit against CW seeks to hold CW accountable under traditional contract law. Exempting private lenders from the consequences of their actions imposed by general contract law is not warranted in this case. In defining the separateness between a private lender, its borrower, and the "guarantor" federal agency, a case from the Sixth Circuit, *Parker v. USDA*, 879 F.2d 1362 (6th Cir. 1989), is on point.

> In 1972, Congress gave the Secretary of Agriculture the authority to guarantee loans made to farmers by private lending institutions. . . . Although the Secretary is permitted to guarantee these loans, whether the loan is actually made is left to the discretion of the lending institution. If a lender elects to make a loan guaranteed by the Secretary through FmHA, the lender must submit a Request for Guarantee form to the FmHA. . . .

> . . . There is no privity of contract between the borrower and FmHA, and the borrower provides no consideration. The borrower is only a party to the contract with the lender[.] . . .
>
> Additionally, the lender is not an agent of FmHA nor is the lender permitted to act as the agent or representative of FmHA. *The funds advanced are those of the lender and not FmHA. FmHA and the lender are completely autonomous organizations* and have no authority to influence the actions of one another.

Id. at 1364-65 (emphasis added).

The choice of whether to apply state or federal law in this type of case has led to confusion and inconsistency in the federal courts. As discussed in Professor Frank S. Alexander's article, *Federal Intervention in Real Estate Finance: Preemption and Federal Common Law*, 71 N.C. L. Rev. 293 (1993), real property law has been the exclusive domain of the states, but with the federal government becoming increasingly involved in real estate finance, the courts have been forced to rely on doctrines of implied preemption and federal common law to determine when and to what extent federal law should displace diverse state real estate finance laws and impose uniformity. "The result has been chaos . . . [and has led to the courts' reaching] inconsistent and unpredictable results . . . in many critical areas." *Id.* at 294.

Thus, even if federal law is generally applicable to HUD-insured loans when defenses are raised against declaration of default or foreclosure by HUD, this is not such a case. West Pointe raised the defenses of waiver and estoppel only against CW, a private lender, based on CW's conduct. This distinction is recognized in *Pankow Construction Co. v. Advance Mortgage Corp.*, 618 F.2d 611 (9th Cir. 1980). In that case, the court, in holding that state law applied to the issues raised in connection with a HUD-insured loan, distinguished the situation where HUD or another federal agency is involved as a party in the case from the situation where only private parties are involved in the dispute, such as the case before it and at issue here. *Id.* at 614 n.7. As the court explained, in such a case there is no

> apparent need for a uniform rule regarding a contractor's remedies against the mortgage lender. No showing has been made that a uniform rule would ease HUD's administrative burdens. And since disputes between the contractor and the mortgage lender over loan proceeds are wholly between private parties, a uniform federal rule is not required to protect the financial interests of the United States.

Id. at 613-14 (footnote omitted). The court then noted that the "noninvolvement of the United States in this case may have a determinative bearing upon the need for a federal common law rule, and suggests a significant distinction between this case and those relied on by [the plaintiff]" in support of his contention that federal law

applied. *Id.* at 614 n.7. Accordingly, the court held that the plaintiff could assert equitable claims against the private lender of a HUD-insured loan. *Id.; see also In re Jack Hudson, Inc.*, 6 B.R. 153 (Bankr. D. Nev. 1980) (in action involving HUD-insured loan, private party was estopped by its conduct and acceptance of the benefits; and holding that the prohibition against assignment of HUD contracts was waived).

Furthermore, the Sixth Circuit opinion in this case is in conflict with other circuits which have held that claims such as waiver and estoppel can modify the terms of a HUD-insured loan, even against HUD. For example, in *Spring Construction Co. v. Harris*, 562 F.2d 933 (4th Cir. 1977), an action against HUD for breach of contract and equitable relief by the prime contractor, the court held that HUD waived any defense of nonperformance it may have possessed where, after it had notice of noncompliance, "it allowed, even encouraged the plaintiff to continue construction, and as a necessary result thereof, plaintiff continued to incur the 10% holdback of contract payments. Defendant encouraged continued construction even though it had knowledge of the very condition which eventually led to the shutdown of the project. In such a situation, HUD will not now be heard to say that the failure of the plaintiff to fully perform the contract bars recovery. Defendant's actions implicitly, if not explicitly, waived such a defense of nonperformance." *Id.* at 936-37 (footnote omitted); *see also Carabetta Enterprises, Inc. v. United States*, 58 Fed. Cl. 563 (2003) (in contract action involving HUD-insured loan, court held that contract was modified by acquiescence of

the plaintiff in the modification by the United States through a course of conduct consistent with acceptance).

Moreover, the Supreme Court has refused to hold conclusively that estoppel never is a defense against the government, *Heckle v. Community Health Services of Crawford County, Inc.*, 467 U.S. 51, 60 (1984), and some circuits have recognized that estoppel may lie against the government in proper circumstances. *See, e.g., United States v. Fox Lake State Bank*, 366 F.2d 962 (7th Cir. 1966); *see also Resolution Trust Corp. v. Van Derweele*, 833 F. Supp. 1383 (N.D. Ind. 1993) (estoppel may apply against Resolution Trust Corporation); *In re Lane*, 96 B.R. 164 (Bankr. C.D. Ill. 1998) (estoppel available against the government where, in addition to traditional elements of estoppel, government has engaged in affirmative misconduct, or a decision in favor of the government would work a manifest injustice; and applying estoppel in government loan contract case).

In light of the foregoing, the Sixth Circuit misapplied the law and erred in concluding that West Pointe could not assert claims of waiver and estoppel against CW. In addition to being in conflict with other circuits, the Sixth Circuit opinion departed from the standards applicable to motions for summary judgment, deprived West Pointe of its right to a jury trial, and worked a substantial injustice on West Pointe. Therefore, this Court should grant West Pointe's petition.

CONCLUSION

For all the foregoing reasons, the Petitioner respectfully requests this Honorable Court to grant this petition and issue a writ of certiorari to the Sixth Circuit Court of Appeals.

Respectfully submitted,

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No._____

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ANN MOSTOLLER, TRUSTEE,

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APPENDIX

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FILED
DEC - 6 2004
LEONARD GREEN,

NOT RECOMMENDED FOR FULL--TEXT PUBLICATION

No. 03-6069

UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

ANN MOSTOLLER, TRUSTEE,	)
	)
Plaintiff-Appellant,	) On Appeal from the United
	) States District Court for the
v.	) Eastern District of Tennessee
	)
CWCAPITAL, LLC,	)
Defendant-Appellee.	)

NOT RECOMMENDED FOR FULL-TEXT PUBLICATION

Sixth Circuit Rule 28(g) limits citation to specific situations. Please see Rule 28(g) before citing in a proceeding in a court in the Sixth Circuit. If cited, a copy must be served on other parties and the Court. This notice is to be prominently displayed if this decision is reproduced.

No. 03-6069
Mostoller v. CWCapital

Before: **BOGGS, Chief Judge; GILMAN, Circuit Judge; and WEBER, District Judge[1]**

PER CURIAM. This is a contract dispute centered on a HUD-backed loan for a housing development. Plaintiff-Appellant Mostoller, Bankruptcy Trustee for West Pointe, appeals from the district court's order granting summary judgment to defendant CWCapital in a suit for breach of contract. Appellant argues that CWCapital breached the contract by declaring West Pointe in default. We find that the contract plainly authorized CWCapital to declare a default if West Pointe failed to meet the construction deadline, and we therefore affirm.

I

On August 7, 1996, West Pointe (now in Chapter 7 and represented by Mostoller), obtained a HUD-insured loan from Continental Wingate ("CW") (CWCapital's predecessor). The loan was to support the construction of a low-to-medium-income residential housing complex, which was to have 33 acres and 150 home units, as well as swimming pools and other facilities. In connection with the loan, the parties executed a number of documents (collectively "loan

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[1]The Honorable Herman J. Weber, Senior United States District Judge for the Southern District of Ohio, sitting by designation.

agreement") governing construction, repayment, and other requirements. The loan agreement required West Pointe to make monthly payments of interest for the first eleven months, and then to repay both interest and principal.

Among other conditions, the loan agreement included two requirements at issue in this case: (1) West Pointe must complete construction by July 7, 1997, and (2) West Pointe must make all payments when due. If West Pointe failed to meet either of these requirements, CW could declare the loan in default. Upon default, CW was authorized to accelerate the loans and demand full repayment immediately. HUD had all responsibility for inspecting the progress of the construction project and determining whether the pace and quality of construction met requirements.

The loan agreement provided that "no waiver by [CW] of any event of default [would] operate as a waiver of any other event of default or the same event of default on a future occasion." Moreover, CW could "delay in exercising or omit to exercise any right or remedy . . . without waiving that or any past, present or future right or remedy." Also, the loan agreement specifically stated that it could be modified only in writing.

A. Problems with Construction (or lack thereof)

West Pointe contracted with Hicks Excavating ("Hicks") to serve as the general contractor on the project.

Hicks was required to finish construction by February 7, 1997, so that West Pointe could begin repaying loan principal by July 7, 1997. Changes to the construction contract had to be approved by HUD and CW in writing.

From an early date, HUD reported slow and problematic construction. In January 1997, West Pointe, with CW's consent, submitted a request to HUD for an additional six-month extension beyond the February 7 deadline in the construction contract. HUD denied the six-month extension, but, in light of rain delays, granted West Pointe an additional eighty-seven days to May 5, 1997. Even with the extension, West Pointe could not complete construction on time. On May 8, 1997, it requested another extension from HUD. In a July 9 letter, HUD's representative stated that "additional time to complete the work has not been justified as required by the general conditions . . . . [M]y staff has not observed a proper, concerted effort . . . to complete the job in a timely manner." Ronald Frye, the president of West Pointe, acknowledged a litany of problems that arose during construction, ranging from unpaved roads to lot grading to faulty piping installation.

Hicks, the general contractor, pulled off the project twice in July and August because of disputes with West Pointe. After Hicks returned briefly, West Pointe kicked Hicks off the work-site in October 1997. After Hicks left the work-site in October, West Pointe was unable to retain another general contractor or induce Hicks to return. At this point the project was about 25% complete.

On November 5, 1997, HUD advised CW that West Pointe may have violated the loan agreement, and recommended that CW not advance further funds and "review the options available to them under default." HUD identified a number of possible violations of the loan agreement by West Pointe, including problems with construction and failure to make required payments.

In addition to the construction problems, West Ponte failed to make full and timely payments on the loan. West Pointe never paid the $23,566 required by HUD as part of a fourth change order. The fourth change order was necessitated by problems with the water piping. HUD approved the change, but required West Pointe to pay the increased costs out of its own pocket by depositing the amount of the cost increase–$23,566–with CW. In addition, West Pointe failed to make the scheduled payment of interest and principal for October 1997. Instead, it submitted a request for an additional advance against the loan.

B. Default and Foreclosure

On December 10, 1997, CW declared West Pointe in default. CW exercised its right to accelerate the loan and demand repayment. Shortly thereafter, CW assigned the loan to HUD, pursuant to HUD regulations.

HUD gave West Pointe several opportunities over the next year to show why HUD should not foreclose. After a full hearing, HUD concluded that the project

could not be salvaged and, on November 9, 1998, declared its intent to foreclose. In the hopes of staying foreclosure, West Pointe filed for bankruptcy. The bankruptcy court, however, granted HUD's request for relief from the automatic bankruptcy stay, and foreclosure proceeded. HUD sold West Pointe's property to the highest bidder for $350,000.

C. Proceedings Below

The Trustee for West Pointe ("West Pointe") brought this suit for breach of contract. West Pointe claimed that HUD and CW were jointly and severally liable for damages resulting from the declaration of default and foreclosure. West Pointe sought $25 million in compensatory damages and $50 million in punitive damages. It alleged that oral modifications of the contract provided for an indefinite extension of construction deadlines. It also alleged that the July 9, 1997, letter from HUD extended the completion date for the project indefinitely.

In its first grant of summary judgment, the district court dismissed as speculative West Pointe's claim for damages associated with "Phase II" of the project. Phase II involved a second parcel of undeveloped land that was adjacent to the land being developed by the HUD-backed loan. At no time was West Pointe the owner of the Phase II land. Although West Pointe had an option to acquire that land, that option expired on August 30, 1997, more than two months before the default. At no time did CW

or any other party agree to finance the development of Phase II. The district court concluded that damages based on Phase II were entirely speculative.

In July 2003, the district court granted summary judgment for CW and HUD on all remaining issues. The district court found that West Pointe had violated the loan agreement in three ways. First, West Pointe failed to complete construction on schedule. Second, it failed to pay the $23,566 required by the change order. Third, it failed to make the required October interest payment.

The district court rejected West Pointe's claim that the contract had been modified. The court concluded that HUD regulations and the terms of the contract prohibited oral modification of the loan agreement. The court also found that any oral modification by a HUD official would be void because that HUD official clearly lacked authority to enter into such modification. Finally, the court found that the July 9 letter, on its face, did not modify the loan agreements. Therefore, West Pointe's failure to complete the project on time was a valid basis to declare it in default.

The court also found that West Pointe violated the contract by failing to pay the interest for October and the $23,566 required by the change order. With respect to the October interest payment, it found that there was "no basis" for West Pointe's claim that another request for an advance on the loan satisfied the payment requirement.

This appeal followed. On appeal, West Pointe has dropped all claims against HUD.[1]

II

We review summary judgment decisions de novo, taking all facts in the light most favorable to the non-moving party. *Michigan Express, Inc. v. United States*, 374 F.3d 424, 426 (6th Cir. 2004). Under the loan agreement, West Pointe was required to complete construction by July 7, 1997. It is undisputed that it did not. It is also undisputed that failure to meet the construction deadline is sufficient basis for a declaration of default. Thus, if the plain terms of the contract apply, CW's declaration of default was not a breach of the contract.

Not surprisingly, West Pointe raises several arguments against applying the plain terms of the loan agreement. At bottom, West Pointe's claim is that by not declaring a default on July 7, 1997–the original deadline for construction–and through its subsequent actions, CW somehow forfeited its rights to make such a declaration later. West Pointe, somewhat vaguely, argues that "[m]any labels" could be applied to this theory, and offers

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[1]West Pointe tried to dismiss HUD as a party late in the proceedings below. The district court issued summary judgment on all remaining issues before considering the motion to dismiss HUD.

modification, waiver, and estoppel as possibilities.[2] These arguments are without merit. Because we believe that West Pointe's failure to meet the construction deadline is dispositive, we need not reach the remaining issues before us.

Federal law governs the interpretation of a HUD-backed loan, and the rights and liabilities of the parties under such a loan. *United States v. Scholnick*, 606 F.2d 160, 164 (6th Cir. 1979) Federal regulations prohibit modification of a federally insured loan except through a written agreement. 24 C.F.R. § 207.256(b). Therefore, doctrines of waiver and estoppel cannot modify the terms of a HUD-insured loan. *United States v. Victory Highway Village, Inc.*, 662 F.2d 488 (8th Cir. 1981). On this basis, courts have consistently held that provisional or informal agreements cannot modify the terms of a HUD-backed loan. *See id.* at 495-98; *Bayvue Apartments Joint Venture v. Ocwen Federal Bank FSB*, 971 F. Supp. 129, 131-32 (D.D.C. 1997) (HUD-insured mortgage cannot be altered by de facto modification doctrine because of the

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[2]However, on appeal, West Pointe abandons its claim of oral modification. Oral modification of a loan is flatly prohibited by the Tennessee Statute of Frauds, Tenn. Code Ann. § 29-2-101(b)(1) (prohibiting oral modifications of a loan contract), and by the plain terms of the contract itself. HUD regulations also require that modifications to HUD-backed loans be in writing. 24 C.F.R. § 207.256(b).

writing requirement of 24 C.F.R. § 207.256(b)). In addition, the plain terms of the loan agreement itself prohibit modification except through a written instrument.

West Pointe argues that the July 9, 1997 HUD letter directed the parties to extend the contractual deadline indefinitely. As the district court noted, the letter plainly does the opposite. The letter begins by identifying that an extension of time–eighty-seven days–has already been granted, but it then states "additional time to complete the work has not been justified."

West Pointe also argues that once the July 7 deadline passed without a declaration of default, the parties were operating under the Extension Agreement, which has no deadline. The Extension Agreement was executed along with other parts of the loan agreement on August 7, 1996. It provides that if construction is not complete by August 7, 1997, West Pointe must pay additional interest fees. The Extension Agreement specifically disclaims any modifications of the deadline or any other requirement in the loan agreement:

> Notwithstanding anything to the contrary set forth herein, Lender's right to receive fees for extending the date of Final Endorsement shall not be construed to give to Mortgagor the right to any extension.... The Obligor acknowledges that Lendor is

> not obligated to grant any extensions by reason of this Agreement and that granting of one or more extensions shall not obligate Lendor to grant any additional or further extensions.

The Extension Agreement expressly does not modify any deadlines and therefore does not support the interpretation given it by West Pointe.

Next we have the somewhat vague waiver and estoppel arguments–these appear to be the same argument in two guises. West Pointe argues that by not declaring default on July 7 and continuing to work on the project, CW waived the construction deadline, or, alternatively, should be estopped from enforcing the construction deadline because West Pointe reasonably incurred costs in the belief that the construction deadline had been indefinitely extended. As we stated above, federal law on this subject is clear: a HUD-guaranteed loan can only be modified in writing. 24 C.F.R. § 207.256(b); *Victory Highway*, 662 F.2d at 495-98. Therefore common law doctrines of waiver and estoppel cannot modify the terms of a HUD-guaranteed loan.

In addition, West Pointe's waiver and estoppel claims are baseless even if we apply Tennessee common law. The only support West Pointe identifies for its claim is the failure to declare default on July 7 and CW's subsequent effort to keep working with West Pointe. The mere failure to declare a default at the earliest possible

date is insufficient to establish an indefinite waiver of that deadline. It is undisputed that CW never told West Pointe that it was extending the deadline or that it would even consider it. West Pointe cites no authority to suggest there is any jurisdiction that would find waiver or estoppel on this basis. We therefore find that West Pointe violated the loan agreement by failing to complete construction as scheduled. CW was thus acting within its contractual rights when it declared West Pointe in default.

III

Because we have determined that CW acted within its contractual rights when it declared West Pointe in default, we need not consider the remaining claims. Since CW did not breach the contract, it is unnecessary to determine whether Phase II damages are speculative. Likewise, it is immaterial whether West Pointe also violated the loan agreement by failing to make required payments. Whether West Pointe failed to meet its contractual obligations in many ways or in only a single way, CW was equally within its rights to declare default. We note, however, that we agree with the district court's analysis with respect to Phase II damages and West Pointe's failure to make required payments.

For these reasons, we AFFIRM the judgment of the district court.

FILED
2003 JUL 18 P 2:04
U.S. DISTRICT COURT
EASTERN DIST. TENN.
BY ___ DEP. CLERK

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF TENNESSEE
AT KNOXVILLE

ANN MOSTOLLER, TRUSTEE,	)	
Plaintiff,	)	
	)	
v.	)	**No. 3:02-CV-291**
	)	**Judge Phillips**
	)	
UNITED STATES OF AMERICA DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT and CONTINENTAL WINGATE ASSOCIATES, INC.,	)	
Defendants.	)	

JUDGMENT ORDER

For the reasons set forth in the memorandum opinion this day filed with the clerk, the motions for summary judgment filed by CWCapital LLC and the Department of Housing and Urban Development [Docs. 66, 76] are **GRANTED**, and this action is **DISMISSED**. The trial scheduled for March 16, 2004 is **CANCELLED**.

IT IS SO ORDERED.

ENTER:

Thomas W. Phillips

Thomas W. Phillips
UNITED STATES DISTRICT JUDGE

Date 7/18/03
Order Book 193 Page 165

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2003 JUL 18 P 2:04
U.S. DISTRICT COURT
EASTERN DIST. TENN.
BY ___ DEP. CLERK

UNITED STATES DISTRICT COURT
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Plaintiff,	)	
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v.	)	**No. 3:02-CV-291**
	)	**Judge Phillips**
	)	
UNITED STATES OF	)	
AMERICA DEPARTMENT OF	)	
HOUSING AND URBAN	)	
DEVELOPMENT and	)	
CONTINENTAL WINGATE	)	
ASSOCIATES, INC.,	)	
Defendants.	)	

MEMORANDUM OPINION

This is a breach of contract claim by the Chapter 7 trustee for West Pointe Properties against Continental Wingate Associates (CW) and the Department of Housing and Urban Development (HUD). Plaintiff seeks compensatory and punitive damages arising from an alleged improper declaration of default under a building

loan agreement between West Pointe and CW involving a HUD insured loan.

Presently pending before the court are motions for summary judgment filed by CWCapital LLC [Doc. 66], and the Department of Housing and Urban Development [Doc.76]. For the reasons which follow, summary judgment will be granted to the defendants and this action will be dismissed.

Background

In 1996, West Pointe obtained a HUD-insured loan from Continental Wingate Associates, Inc., CW's predecessor, in the amount of $2,222,900.00 pursuant to the Section 207 Program, for the purposes of developing and constructing a mobile home park. In connection with the loan, West Pointe executed a Deed of Trust Note (Note), a Deed of Trust, a Security Agreement, a Building Loan Agreement, a Regulatory Agreement and various other documents required by HUD as a condition of insuring the loan (collectively the "Loan Documents"). Through the Loan Documents, CW, after permission and authorization from HUD, agreed to advance construction funds to West Pointe to build the project. The Note obligated West Pointe to repay the loan pursuant to a fixed schedule with interest only due for the first eleven months and principal and interest due each month thereafter. The Note was secured by a Deed of Trust, which placed a first lien on the project and provided various remedies in the event of a default. The Deed of Trust indicates that a default under either the Building Loan Agreement or the Regulatory Agreement constitutes a default under the Deed of Trust.

Pursuant to the Building Loan Agreement, West Pointe was required to complete construction of the project by July 7, 1997, eleven months after the loan closing. The Construction Contract that West Pointe signed with its general contractor, however, provided for a shorter construction period to ensure that West Pointe's obligations under the Loan Documents could be fulfilled. The Construction Contract provided that any changes therein had to be approved in writing by CW and HUD. In addition, the Construction Contract provided that "[t]he time by which the work shall be completed may be extended in accordance with the terms of said AIA General Conditions only with the prior written approval of the Commissioner [HUD]." West Pointe acknowledged in the Building Loan Agreement that failure to complete the project by July 7, 1997 or cessation of work on the project for a period of more than 20 days (among other things) constituted defaults. In addition, the Security Agreement, through which West Pointe pledged the project and certain other property as collateral for the loan, specifies various events of default including failure to make a payment when due, a default or breach of any of the Loan Documents, and any representation or warranty made by West Pointe in connection with the loan being false.

Upon an event of default, CW was authorized to accelerate the loan and declare a default. The Security Agreement signed by the parties states that "no waiver by the Secured Party of any event of default [would] operate as a waiver of any other event of default or of the same event of default on a future occasion." Moreover, the Secured Party could "delay in exercising or omit to exercise any right or remedy . . . without waiving that or

any past, present or future right or remedy." The Security Agreement also contained a prohibition against oral modifications in that it stated it "may not be amended, altered or changed other than in a writing signed by" CW and West Pointe because the Security Agreement and the other "Loan Documents represent the entire agreement between [CW] and [West Pointe]." Finally, at closing, West Pointe executed a certification of Mortgagor that certified that "the terms and conditions of the loan as reflected in the Loan Documents have not been amended, modified or supplemented, directly or indirectly, by any other agreement or understanding of the parties or waiver of any of the material provisions of the Loan Documents."

From almost the beginning of the project problems arose with the progress of construction. Under the Loan Documents, the responsibility for inspecting the progress of completion and conformity of the construction work was vested entirely with HUD. HUD inspection reports from an early date reflected slow and problematic construction. In January 1997 West Pointe submitted a request fora six-month extension of the completion date. HUD denied in writing the request for the six-month extension and permitted only an additional 87 days for rain delays. West Pointe failed to complete the construction within the time allotted. On May 8, 1997, West Pointe submitted a second extension request, which was also rejected by HUD in writing on July 7, 1997. In a letter dated July 9, 1997, HUD's representative, William McClister, stated that "additional time to complete the work has not been justified as required by the general conditions. . . . my staff has not observed a proper, concerted effort . . . to complete this job in a timely

manner." No extension could be given without HUD's approval. The general contractor pulled off the job in July and then again in October 1997 following a dispute with West Pointe. At that point, the project was only 25-30% complete.

In addition to the construction problems, West Pointe failed to make payments due under the Loan Documents. First, West Pointe failed to pay $23,566 to keep the HUD loan in balance pursuant to the conditional approval of a change order by HUD. In addition, West Pointe repeatedly failed to make timely payments on the Note. Finally, West Pointe failed to make payment of interest and escrows due in the amount of $9,789.68 to cover the month of October 1997.

On November 5, 1997, HUD advised CW that West Pointe "may have violated various provisions of the Building Loan Agreement and directed CW's attention to the remedies available to the lender in the case of a default by the borrower. By letter, HUD directed CW to declare a default and foreclose the loan. As a result of the monetary and construction-related defaults, on December 10, 1997, CW declared the loan in default and exercised its right pursuant to the Loan Documents to accelerate the loan. Thereafter, CW assigned the loan to HUD in accordance with HUD regulations.

After CW assigned the loan to HUD, all rights and duties of CW were transferred from CW to HUD. On February 18, 1998, after CW had assigned the loan to HUD, HUD notified West Pointe that CW had assigned the mortgage to HUD; that the entire indebtedness, as accelerated by CW, was due and payable; and that HUD

would proceed with foreclosure unless West Pointe remitted the amount payable within thirty days. On March 23, 1998, HUD notified West Pointe that the funds necessary to avoid foreclosure had not been received and that HUD would provide West Pointe with an opportunity to show reasons why foreclosure should not take place. On May 14, 1998, West Pointe's principle and counsel met with HUD staff in Atlanta. On November 9, 1998, HUD notified West Pointe that the agency had considered all of the materials and allegations advanced by West Pointe regarding not proceeding with foreclosure, and West Pointe had presented no legal reasons to alter HUD's decision to foreclose. HUD held the loan for over a year and a half before publishing a foreclosure notice with the sale scheduled for May 27, 1999. West Pointe filed bankruptcy in order to prevent the foreclosure. The bankruptcy court granted HUD's motion for relief from the automatic stay and permitted HUD to foreclose on the property. In granting relief from the stay, the bankruptcy court stated that it was "undisputed that the Debtor (West Pointe) had made no principal payments on the August 7, 1996 Deed of Trust Note since its inception; that the Debtor had no income; . . . and that the Debtor last performed work on the property in late October 1997." On April 27, 2000, HUD foreclosed on West Pointe's mortgage. HUD sold the West Pointe property to the highest bidder at a price of $350,000.

The Trustee for West Pointe claims damages as a result of the foreclosure by HUD. West Pointe asserts that CW should not have declared the loan in default contending that the Building Loan Agreement was modified by oral representations providing for an

"indefinite" extension of the construction deadline. In the alternative, West Pointe asserts that a letter from HUD dated July 9, 1997, extended the completion date for the project and that CW and HUD breached that agreement by foreclosing. West Pointe seeks $25,000,000 in damages for lost profits jointly and severally against CW and HUD. In addition, West Pointe seeks $50,000,000 in punitive damages against the defendants. CW and HUD move for summary judgment in their favor asserting that as a matter of law the Loan Documents could not be orally modified, the Loan Documents were not in fact modified, and neither CW nor HUD breached any contractual duties to West Pointe. Thus, CW and HUD assert that judgment should be rendered in their favor as a matter of law on the trustee's claims.

Applicable Law

Rule 56(c), Federal Rules of Civil Procedure, provides that summary judgment will be granted by the court only when there is no genuine issue of material fact and the moving party is entitled to judgment as a matter of law. The burden is on the moving party to conclusively show that no genuine issue of material fact exists. The court must view the facts and all inferences to be drawn therefrom in the light most favorable to the non-moving party. *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587 (1986); *Morris to Crete Carrier Corp.*, 105 F.3d 279, 280-81 (6th Cir. 1987); *White v. Turfway Park Racing Ass'n, Inc.*, 909 F.2d 941, 943 (6th Cir. 1990); *60 Ivy Street Corp. v. Alexander*, 822 F.2d 1432, 1435 (6th Cir. 1987). Once the moving party presents evidence sufficient to support a motion under Rule 56, Federal Rules of Civil Procedure, the non-moving party is not

entitled to a trial simply on the basis of allegations. The non-moving party is required to come forward with some significant probative evidence which makes it necessary to resolve the factual dispute at trial. *Celotex Corp. v. Catrett*, 477 U.S. 317 (1986); *White*, 909 F.2d at 943-44. The moving party is entitled to summary judgment if the non-moving party fails to make a sufficient showing on an essential element of its case with respect to which it has the burden of proof. *Celotex*, 477 U.S. at 323; *Collyer v. Darling*, 98 F.3d 220 (6th Cir. 1996).

The National Housing Act (NHA) prohibits the oral modification of mortgage agreements. The NHA states in pertinent part that:

> The Secretary shall not consent to any request for curing a default under any mortgage covering multifamily housing... or for a modification of the terms of such mortgage, except inconformity with regulations prescribed by the Secretary in accordance with the provisions of this section.

12 U.S.C. § 1715z-4.

Every court that has examined an alleged oral modification of a HUD loan agreement has specifically refused to enforce alleged oral modifications of mortgage agreements based on the NHA's prohibitions. *See VS Ltd. Partnership v. Dep't of Housing & Urban Development*, 235 F.3d 1109, 113 (8th Cir. 2000) ("The NHA . . . specifically prohibits the oral modification of mortgage agreements."); *Bayvue Apts. Joint Venture v. Ocwen*

Federal Bank FSB, 971 F. Supp. 129, 131 (D.D.C. 1997) ("neither federal or [state] law permits the enforcement of an agreement that was unwritten"); *Teitlebaum v. HUD*, 953 F. Supp. 326, 331 (D. Nev. 1996) ("The NHA does not give the Secretary [i.e. HUD] authority to orally modify the terms of a mortgage loan.").

In addition, regulations established by HUD in accordance with Section 1715z-4 require all modifications of a mortgage agreement be made only when the parties reach such terms in writing. See 24 C.F.R. § 207.256b; 24 C.F.R. § 221.761(a)(2); *see also VS Ltd. Partnership*, 235 F.3d at 1113 ("HUD regulations permit modification of a mortgage agreement only with the approval of [HUD], and allow that only when the parties reach terms in writing"); *Teitlebaum*, 953 F. Supp at 331 ("Furthermore, the regulations prescribed by [HUD] in accordance with Section 1715z-4 require all mortgage modifications be made pursuant to the written approval of [HUD]"); *Kent Farm Co. v. Hills*, 417 F. Supp. 297, 303 (D.D.C. 1976) ("These statutes and regulations clearly create limited circumstances under which workout arrangements are possible. But within that range, the discretion of [HUD] to approve a plan is, as a practical matter, absolute. Plaintiff has no right to such an agreement under the statute or regulations").

Analysis

The basis of the trustee's complaint is that HUD, CW and West Pointe verbally modified the loan documents and that West Pointe has suffered damages as a result of the failure of HUD and CW to honor the alleged oral modifications. CW and HUDmove the court

for summary judgment stating that as a matter of law, the alleged oral agreement for an extension of time to complete the project was never enforceable because the National Housing Act prohibits the enforcement of an agreement that is not in writing. Moreover, written approval to modify the loan documents must come from the Federal Housing Commissioner. Finally, defendants assert that the law is clear that oral modifications by HUD representatives who lack authority to make such agreements are unenforceable as a matter of law.

West Pointe argues that the loan documents were orally modified. West Pointe asserts that Arlin Reynolds at HUD's Knoxville office told West Pointe's representative that HUD was willing to authorize modification of the loan documents to extend the construction period. West Pointe further asserts that Reynolds stated that he had already discussed this with a CW loan official who on behalf of CW had agreed to extend the completion date on the project.

West Pointe does not claim that the Commissioner of HUD approved any modifications to the Loan Documents. Nor does West Pointe contend that any of the parties to any of the Loan Documents put the terms of the purported oral modifications in writing. As a borrower with experience with HUD loans, West Pointe was well aware that any such modifications of the Loan Documents had to be in writing. Accordingly, the court finds that West Pointe's purported oral modification to the Loan Documents is specifically prohibited under the NHA.

Moreover, courts will not enforce agreements made by individuals without actual authority to make such agreements. Where such agreements are made, the terms of such agreements have been rendered void. West Pointe has the burden of showing that officials who made the alleged agreement had the authority to commit the Government. *Jascourt v. United States*, 207 Cl. Ct. 955, *cert. denied*, 423 U.S. 1032 (1975). Statements by officials of HUD "cannot bind the United States or work an estoppel against its exercise of a right clearly defined in the statute and reserved in the mortgage(s)." *United States v. Wennick*, 645 F. Supp. 103, 106 (D. Del. 1986). Indeed, where HUD representatives lacked authority to make modifications to the agreement, such modifications were void. *See Lehner v. United States*, 1 Cl. Ct. 408 (1983); *see also Bayvue Apts.*, 971 F. Supp at 131-32.

The HUD regulations clearly indicate that only the Federal Housing Commissioner can modify a loan document. Any claim by West Pointe that local HUD representatives had apparent or actual authority to make oral modifications to the Loan Documents fails as a matter of law because the NHA makes it abundantly clear that the individuals who West Pointe claimed to have relied upon for the oral modification to the Loan Documents did not have actual authority to reach such an agreement. Therefore, as a matter of law, no oral modification could exist.

Even if the court were to construe the alleged oral modification as a provisional work-out agreement, such work-out agreement does not modify or supercede the original loan agreements as a matter of law and any such work-out agreement must be narrowly construed. The

case law states that borrowers have no "right" to a provisional work-out agreement. In instances where a provisional work-out agreement has been created "it is well established that such provisional work-out agreements do not modify or supersede the original mortgages and mortgage notes or alter HUD's rights to foreclosure on default." *Multifamily Mortgage Trust 1996-1 v. Century Oaks Ltd.*, 532 S.E.2d 578, 582 (N.C. 2000) *quoting United States v. Wennick*, 645 F. Supp. 103, 105 (D. Del. 1986); *see also United States v. Victory Highway Village, Inc.*, 662 F.2d 488 (8th Cir. 1981); *United States v. 1300 Lafayette East*, 455 F. Supp. 988, 991 (E.D. Mich. 1978); *United States v. Woodland Terrace Inc.*, 293 F.2d 505 (4th Cir.), *cert. denied*, 368 U.S. 940 (1961).

As for West Point's assertion that the Loan Documents were modified in writing by the July 9, 1997 letter from HUD, the letter on its face does not constitute an amendment to the Loan Documents. The letter states in pertinent part as follows:

> Enclosed is form HUD-92437, Request for Construction Changes on Project Mortgages, Number 3, for the subject project which is marked unacceptable. Please note that an extension of 87 days to May 5, 1997, was granted by change order number 2 to cover loss of work time due to inclement weather. Additional time to complete the work has not been justified as required by the general conditions. Also my staff has not observed a proper, concerted effort on the part of the general

contractor to complete this job in a timely manner.

Based on the above situation, the liquidated damages clause in the construction contract must be relied on as a source of funds for potential overruns in interest, taxes, mortgage insurance premium, and property insurance. Under provisions of HUD Handbook 4435.1 REV-1, paragraph 4-5 C., I have authorized the transfer of funds from the construction account to cover these soft costs to an assumed revised completion date of September 30, 1997. . . .

Initially this amount will be allocated to cover the construction interest to the final inspection date and interest to the cut off date. Due to the nature of a 207(m) project, this Office has taken the position that it is very important to maintain adequate interest and other soft costs during the period from final inspection to the cut off date (up to five months).

This transfer is a minimum at this time to cover soft cost expenses. The actual amount of the reduction in the contract sum for late completion of the project is the lesser of actual damages or $769.12 for each day of delay as set forth in Article 2 of the construction contract. This computation is

reduced by any net operating income during the damage period.

West Pointe asserts that this letter constitutes a modification of the loan documents extending the time for completion of the project. West Pointe's assertion is without merit. The July 9 letter fails to meet any of the criteria set out above under the NHA for a valid modification. First, it does not indicate that it constituted an amendment. Second, it is not signed by CW, the lender and party to the Loan Documents. Third, West Pointe has not established that the sender of the letter, William McClister, had authority to commit the government. West Pointe has the burden of showing that a written modification of the Loan Documents existed and that the official who allegedly made the agreement had the authority to commit the government. West Pointe fails to establish either point.

West Pointe further contends that CW had discretion under the Loan Agreement to terminate the agreement after July 7, 1997 due to West Pointe's failure to complete the project by that date, but CW waived that right by its failure to immediately declare the loan in default. This contention is also without merit.

The Security Agreement provides that:

> [n]o waiver by the Secured Party of any Event of Default under this Agreement will operate as a waiver of any other Event of Default or of the same Event of Default on a future occasion. The Secured Party may delay in exercising or omit to exercise any

> right or remedy under this Agreement or under any other Loan Document without waiving that or any past, present or future right to remedy.

Clearly, if the Loan Documents cannot be amended without a writing signed by all the parties, there can be no waiver absent a written agreement indicating as such. Thus, an unwritten waiver of a right contained in the Loan Documents is prohibited as a matter of law and contract and West Pointe has failed to establish any waiver.

Even if the court accepted that the July 9 letter "assumed [a] revised completion date of September 30, 1997, West Pointe was still in default of any assumed completion date. It was not until December 1997 that CW ultimately declared the loan in default and initiated the assignment to HUD. At that point, West Pointe had failed to complete the project in accordance with the schedules and was not even remotely close to finishing the project, West Pointe was without a general contractor, and was not progressing with the work.

The evidence shows that West Pointe also failed to make payments as required under the Loan Documents: (1) West Pointe failed to pay interest due for October1997; and (2) West Pointe failed to fund a change order as required by the Loan Documents. West Pointe argues that payment was satisfied by West Pointe's request for an advance of money from CW for these payments. There is no basis in the loan documents for West Pointe's position.

The Note explicitly states that "commencing on the first day of August 1997, installments of interest and principal shall be paid in the sum of Sixteen Thousand Five Hundred Fifty and 07/100 Dollars each . . . until the entire indebtedness has been paid." Nowhere in the Loan Documents does it indicate that West Pointe is excused from paying the interest. While the Building Loan Agreement permits the borrower to seek advances from the loan to make certain payments that become due, it requires the borrower "to make application at least 15 days before the date the advance is desired" and predicates the borrower's receipt of such advance upon the approval of both the lender and HUD. Moreover, if the loan was not in balance or if there were other defaults, the Loan Documents prohibited additional advances from the loan. It was West Pointe's obligation to keep the loan in balance and West Pointe's obligation to pay for any change orders outside of the scope of the agreements.

It is undisputed that the Loan Documents required the construction of the project to be completed prior to July 1997. It is also undisputed that the construction was less than 30% complete as of that date. It is, likewise, undisputed that West Pointe was required to make certain payments on the Note pursuant to the Loan Documents, and that West Pointe failed to make such payments to CW. Pursuant to the terms of the Loan Documents, these breaches of the Loan Documents each constituted a default. Per HUD's recommendation, CW declared the loan in default on December 10, 1997. Even after CW assigned the loan to HUD, HUD did not foreclose for over a year and a half. At any point prior to

HUD's foreclosure, West Pointe could have cured the default or submitted a work-out plan for the loan.

It is the conclusion of the court that as a matter of law the Loan Documents could not be orally modified. Further, the court finds that the Loan Documents were not modified by the July 9, 1997 letter from HUD. Thus, neither CW nor HUD breached any contractual duties to West Pointe and summary judgment will be granted to CW Capital LLC and the Department of Housing and Urban Development.

Conclusion

For the reasons stated above, the motions for summary judgment filed by CWCapital LLC [Doc. 66], and the Department of Housing and Urban Development [Doc.76] will be **GRANTED**, and this action will be **DISMISSED**.

ENTER:

Thomas W. Phillips

Thomas W. Phillips
UNITED STATES DISTRICT JUDGE

FILED
MAR 6 10 05 AM '03
U.S. DISTRICT COURT
EASTERN DIST. TENN.
BY ___ DEP. CLERK

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF TENNESSEE
AT KNOXVILLE

ANN MOSTOLLER, TRUSTEE,	)	
Plaintiff,	)	
	)	
v.	)	**No. 3:02-CV-291**
	)	**Judge Phillips**
	)	
UNITED STATES OF AMERICA DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT and CONTINENTAL WINGATE ASSOCIATES, INC.,	)	
Defendants.	)	

MEMORANDUM AND ORDER

This is a breach of contract claim by the Chapter 7 trustee for West Pointe Properties against Continental Wingate Associates (CW) and the Department of Housing and Urban Development (HUD). Plaintiff seeks compensatory and punitive damages arising from an alleged improper declaration of default under a building

loan agreement between West Pointe and CW involving a HUD insured loan.

Presently pending before the court are the following motions: (1) defendant Continental Wingate's motion for partial summary judgment [Doc. 17]; (2) defendant United States' motion to continue trial date [Doc. 21]; (3) plaintiff's motion for separate trials [Doc. 30]; (4) motion of West Pointe Development to quash subpoena [Doc. 34]; and (5) plaintiff's motion for voluntary dismissal [Doc. 52]. A hearing was held on these motions on January 24, 2003. Following the hearing, defendant Continental Wingate filed a second motion for summary judgment [Doc. 66] and a motion requesting the court to consider and resolve defendant's second motion for summary judgment prior to consideration of the partial motion for summary judgment and plaintiff's motion for voluntary dismissal [Doc. 68].

1

CWCapital LLC (CW), successor to defendant Continental Wingate Associates, moves the court for partial summary judgment on plaintiff's claim for damages relating to Phase II of the West Pointe mobile home park development [Doc. 17]. In support of its motion, CW states that the parties' contractual relationship did not encompass Phase II of the West Pointe development, and further, West Pointe never owned the property upon which Phase II was to be developed. Therefore, CW argues it cannot have any responsibility, as a matter of law, for damages relating to Phase II.

Plaintiff responds in opposition, stating that the West Pointe mobile home park was to be developed in two phases. When CW terminated the loan for Phase I, West Pointe lost the opportunity to develop both phases. Therefore, plaintiff argues, West Pointe is entitled to lost profits due to the wrongful termination of the West Pointe project as a whole since West Pointe's opportunity to develop Phase II and make profits was lost.

Facts

West Pointe was the owner/developer of a mobile home park located in Knox County, Tennessee. The project was financed by CW pursuant to a building loan agreement which was insured by HUD. The real estate upon which Phase I of the development was to have been constructed was a 32 acre parcel of undeveloped land which was part of the collateral security for the loan by CW to West Pointe. Phase II was to be built upon a 29 acre parcel of undeveloped land contiguous to the Phase I land. This 29 acre parcel was owned by West Pointe II, a separate Tennessee limited partnership.

Approximately three weeks after the August 7, 1996 loan closing between West Pointe, CW and HUD, West Pointe II transferred, by quit claim deed, the Phase II real estate to J. Hicks Excavating, Inc., a contractor for the site work on Phase I. At no time has West Pointe been the record title owner of the Phase II real property, and CW did not make a loan or loan commitment to West Pointe for the Phase II development.

Applicable Law

The court, when exercising diversity jurisdiction over a breach of contract claim, is required to apply Tennessee law regarding proof of damages. *See Erie R.R. v. Tompkins*, 304 U.S. 64 (1938). Under Tennessee law, the purpose of awarding damages in breach of contract actions is to compensate for damages actually incurred by placing the plaintiff in the position he would have occupied had the contract been fulfilled in accordance with its terms, *Corporate Air Fleet v. Gates Learjet, Inc.*, 589 F. Supp. 1076, 1082 (M.D. Tenn. 1967), *aff'd*, 406 F.2d 731 (6th Cir. 1969) (per curium); *Action Ads, Inc. v. William B. Tanner Cor.*, 592 S.W.2d 572, 575 (Tenn. App. 1979), not to provide a windfall for the plaintiff. *See Great American Music Mach., Inc. v. Mid-South Record Pressing Co.*, 393 F. Supp. 877, 885 (M.D. Tenn. 1975); *Action Ads*, 592 S.W.2d at 575. The plaintiff bears the burden of proving damages, *see Volasco Products Co. v. Lloyd A. Fry Roofing Co.*, 308 F.2d 383, 392 (6th Cir. 1962), *cert. denied*, 372 U.S. 907 (1963); *Cecil Corley Motor Co. v. General Motors Corp.*, 380 F. Supp. 819, 854 (M.D. Tenn. 1974), and without adequate proof, there can be no award of damages in any amount. *See Cecil Corley Motor Co.*, 380 F. Supp at 858; *Inman v. Union Planters Nat'l Bank*, 634 S.W.2d 270, 272, (Tenn. App. 1982).

As a general rule, "damages are not permitted which are remote and speculative in nature." *Agricultural Services Ass'n v. Ferry-Morse Seed Co.*, 551 F.2d 1057, 1072 (6th Cir. 1977); *see also Maple Manor Hotel, Inc. v. Metropolitan Gov't of Nashville & Davidson County*, 543 S.W.2d 593, 598-99 (Tenn. App. 1975); *Anderson-Gregory Co. v. Lea*, 370 S.W.2d 934, 937 (Tenn. 1963). This rule

serves to preclude recovery, however, only where the fact of damage is uncertain, *i.e.*, where the damage claimed is not the certain result of the wrong, not where the amount of damage alone is uncertain. *Coverdell v. Mid-South Farm Equip. Ass'n*, 335 F.2d 9, 14 (6th Cir. 1964); *Redbud Coop. Corp. v. Clayton*, 700 S.W.2d 551, 561 (Tenn. App.1985); *Cummins v. Brodie*, 667 S.W.2d 759, 765 (Tenn. App. 1983); *Acuff v. Vinsant*, 443 S.W.2d 669, 674 (Tenn. App. 1969). Once the existence of damages has been shown, all that an award of damages requires is substantial evidence in the record to permit a factfinder to draw reasonable inferences and make a fair and reasonable assessment of the amount of damages. *Lee Shops Inc. v. Schatten-Cypress Co.*, 350 F.2d 12, 18 (6th Cir. 1965), *cert. denied*, 382 U.S. 980 (1966); *Coverdell*, 335 F.2d at 14; *Redbud Coop. Corp.*, 700 S.W.2d at 561; *Cummins*, 667 S.W.2d at 765.

Specifically, Tennessee law permits lost profits to be recovered following a breach of contract. *Booker v. Ralston Purina Co.*, 699 F.2d 334, 336 (6th Cir. 1983); *Lee Shops*, 350 F.2d at 18; *Morristown Lincoln-Mercury Inc. v. Roy N. Letspeich Publishing Co.*, 298 S.W.2d 788, 793 (Tenn. App. 1956). As with any other damages, however, the particular lost profits being claimed in any given case must not be remote, uncertain, or speculative by their very nature, *see, e.g., Clark v. Ferro Corp.*, 237 F. Supp. 230, 238-40 (E.D. Tenn. 1964); *American Bldgs Co. v. DBH Attachments, Inc.*, 676 S.W.2d 558, 562-63 (Tenn. App. 1984). Lost profits will be denied if it is uncertain that the defendant's breach caused the loss, *Lawler v. Zapletal*, 679 S.W.2d 950, 953 (Tenn. App. 1984), or uncertain that the plaintiff would have made a profit in the absence of a breach. *See, e.g., Great American Music Mach.*, 393 F. Supp at 885; *Morristown Lincoln-Mercury*, 298 S.W.2d at 793.

Moreover, even if the existence of lost profits is established, recovery is properly denied if the plaintiff fails to provide a "sufficient basis for the jury's computation of the damage," *Bigelow v. RKO Radio Pictures, Inc.*, 327 U.S. 251 (1946), by "furnishing data from which the amount of the probable loss could be ascertained asa matter of reasonable inference," *Eastman Kodak Co. v. Southern Photo Materials Co.*, 273 U.S. 359, 379 (1927), and "determined with reasonable certainty," *Volasco Products Co.*, 308 F.2d at 392; *Cecil Corley Motor Co.*, 380 F. Supp. at 854. A plaintiff clearly fails to prove the amount of lost profits with reasonable certainty by merely claiming that he could have sold a given number of products at a stated profit. *See Burge Ice Mach. Co. v. Strother*, 273 S.W.2d, 479 (Tenn. 1954); *Morristown Lincoln-Mercury*, 298 S.W.2d at 794-95.

In addition, summary judgment is only appropriate when there are no genuine issues of material fact and the moving party is entitled to judgment as a matter of law. Fed. R. Civ. P. 56(c). The party seeking summary judgment bears the initial burden of showing the district court that there is an absence of a genuine dispute over any material fact. *Celotex Corp. v. Catrett*, 477 U.S. 317, 323 (1986). This burden may be discharged either by producing evidence showing the absence of a genuine issue of material fact or by showing that there is an absence of evidence to support the nonmoving party's case. *Id.* at 325. Once the moving party has made and supported its motion for summary judgment, the adverse party must, by affidavits or otherwise, set forth specific facts showing that there is a genuine issue for trial. Fed. R. Civ. P. 56(e). "The mere existence of a scintilla of evidence in support of the plaintiff's position will be

insufficient; there must be evidence on which the jury could reasonably find for the plaintiff." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 252 (1986). Where, looking to the record as a whole, a reasonable mind could come to only one conclusion, there is no genuine issue of material fact and summary judgment is appropriate. *Anderson*, 477 U.S. at 250-51.

Applying the foregoing principles, I cannot find that defendant's alleged breach of contract resulted in any loss of profits to plaintiff from the Phase II property. First, West Pointe never owned the real property upon which Phase II was to be constructed. Plaintiff does not dispute the fact that West Pointe II is a separate legal entity that owned title to the Phase II property, and that record title to the Phase II property was conveyed to J.W. Hicks Excavating shortly after CW made the loan at issue in this case. Second, CW did not have a contractual relationship with West Pointe II as neither HUD nor CW made a loan or a loan commitment relating to the Phase II property. Third, the contract by which the Phase II property was conveyed to J. Hicks Excavating is a contract with West Pointe II, not the debtor West Pointe, and West Pointe II was the entity that was entitled to repurchase the property. Lastly, the terms of the contract by which West Pointe II was entitled to repurchase the property specifically provided that the right to repurchase expired on August 30, 1997, more than two months before the notice of default in this case. Therefore, I find that any damages for Phase II of the development were too remote to have reasonably been within the contemplation of the parties at the time the contract was made.

The law is well settled that the injured party is not to be put in a better position by a recovery of damages for breach of contract than he would have been in if there had been full performance. *Great American Music Mach.*, 393 F. Supp. at 885; 25 C.J.S. Damages §3. Moreover, "a party who has failed to fulfill a contract cannot be held liable for remote, contingent and uncertain consequences, or for speculative or possible results which may have ensued on his breach of duty, although they may be traceable to that cause." *Baker v. Riverside Church*, 453 S.W.2d at 810. Since West Pointe did not own the Phase II property and defendant did not have a contract with West Pointe II, defendant had no duty to West Pointe II, no duty was breached, and no damages proximately resulted to West Pointe from any action or inaction of defendant relative to the Phase II property.

Further, in order for CW to have any potential liability for damages relating to Phase II, several contingencies would have to occur: West Pointe would need to acquire the funds to purchase the Phase II property; West Pointe would have to obtain the funding for development of Phase II; and West Pointe would have to acquire residents for Phase II. These contingencies, relied on by West Pointe to support a claim for damages relating to the Phase II property are based on speculation and are so uncertain in character that a judgment cannot be reasonably based on the same. Plaintiff has offered nothing but speculation about what might have occurred had CW not terminated the loan for Phase I of the development. Speculation about what might have occurred fails to create a jury question as to the alleged damage sustained by plaintiff for Phase II of the project. *See Spalding v. Davis*, 674 S.W.2d 710, 715 (Tenn. 1984),

overruled in part on other grounds, Meadows v. State, 849 S.W.2d 752 (Tenn. 1993).

Moreover, it appears that the bankruptcy trustee for West Pointe has no standing to pursue a claim relating to property that was not part of the bankruptcy estate. "[A] trustee cannot recover that which did not belong to the estate at the time the debtor filed for bankruptcy protection." *In re Bean*, 252 F.3d 113 (2d Cir. 2001); *see also*, 11 U.S.C. § 541 (defining property of the estate). Since neither the Phase II property, nor a claim by West Pointe II, were assets acquired by the trustee herein, it is clear that standing does not exist.

For the foregoing reasons, it is the opinion of the court that CW is entitled to judgment as a matter of law as to plaintiff's claim for damages relating to Phase II of the West Pointe development. Accordingly, CW's motion for partial summary judgment [Doc. 17] is **GRANTED**.

II

Defendant HUD has moved to continue the trial of this matter, currently scheduled to begin February 19, 2003 [Doc. 21]. Plaintiff and defendant CW do not oppose the requested continuance [Docs. 26, 33]. Accordingly, the trial of this case is continued and shall commence at **9:00 a.m. on September 8, 2003**. A final pretrial conference is scheduled for **9:00 a.m. on September 3, 2003**. The trial is expected to last five days.

The court notes that this case was previously assigned to the Honorable James H. Jarvis, who directed

the Bankruptcy Court to conduct all pretrial matters [Doc. 5]. The parties are advised that the undersigned will conduct all future hearings in this case and the orders of the Honorable Richard Stair, Jr., Bankruptcy Judge, in this case are affirmed and adopted by the undersigned. Further, the parties are **DIRECTED** to make all future filings with the clerk of this court in Ann Mostoller v. United States of America Department of Housing and Urban Development and Continental Wingate Associates, Inc., Case No. 3:02-CV-291.

III

Plaintiff has moved the court for an order allowing the issues pertaining to each defendant to be tried separately [Doc. 30]. Defendant CW opposed the motion stating that the evidence relating to both defendants will significantly overlap and that severing the cases would create two multi-day trials [Doc. 38].

Rule 42, Federal Rules of Civil Procedure, allows the court to order a separate trial of any claim "in furtherance of convenience or to avoid prejudice, or when separate trials will be conducive to expedition and economy." Plaintiff has not shown a basis for separate trials. In the opinion of the court, matters of judicial economy require trial of both causes of action at the same time. Accordingly, plaintiff's motion for separate trials [Doc. 30] is **DENIED**.

IV

West Pointe, a nonparty to this action, has moved the court for an order quashing the subpoena of its bank

records that was issued to AmSouth Bank on December 2, 2002. In support of its motion, West Pointe states that the subpoena is unduly burdensome and seeks the discovery of confidential commercial information that is neither relevant nor material to this matter nor likely to lead to the discovery of admissible material evidence in this case [Doc. 34].

CW has responded that it is agreeable to a reasonable protective order that would protect the dissemination of information and documentation obtained by virtue of the subpoena (deemed "confidential commercial information") for use only in connection with CW's defense of the trustee's lawsuit. CW points out that the bank from which the records were subpoenaed has not interposed any objection that the request is unduly burdensome. Moreover, CW contends that the sought information is relevant because any damages suffered by West Pointe were because of the surreptitious and improper diversion of funds from West Pointe to its general partner or to the president of the general partner [Doc. 37].

It appears that the information sought from AmSouth Bank is relevant and material. Accordingly, the deposition may go forward; however, a protective order will be entered in this matter. Any information obtained during the course of the deposition shall not be disclosed to any third parties without the prior approval of this court. All counsel participating in this case will be subject to the protective order. The parties are **DIRECTED** to prepare and file with the court a suitable order incorporating the appropriate provisions.

Accordingly, the motion of West Pointe to quash the subpoena [Doc. 34] is **DENIED**.

V

Plaintiff has moved the court for entry of an order voluntarily dismissing HUD from this lawsuit [Doc. 53]. HUD does not object to the motion [Doc. 64]; however, CW has filed a response opposing the voluntary dismissal of HUD from this case [Doc. 69]. In addition, CW has filed a second motion for summary judgment [Doc. 66] and a motion requesting the court to consider and resolve defendant's second motion for summary judgment prior to consideration of the partial motion for summary judgment and plaintiff's motion for voluntary dismissal [Doc. 68]. Defendant's motion requesting the court to stay consideration of the pending motions will be **GRANTED IN PART AND DENIED IN PART**. The motion to stay consideration on the partial motion for summary judgment is **DENIED**; and the motion to stay consideration of plaintiff's motion for voluntary dismissal is **GRANTED**. Plaintiff is directed to file a response to CW's motion for summary judgment on or before **April 1, 2003**. The court will hear oral argument on the motion for summary judgment on **April 25, 2003 at 9:00 a.m.**

IT IS SO ORDERED.

ENTER:

Thomas W. Phillips

Thomas W. Phillips
UNITED STATES DISTRICT JUDGE

(2)

Supreme Court, U.S.
FILED
MAY 11 2005
OFFICE OF THE CLERK

No. 04-1208

IN THE

Supreme Court of the United States

ANN MOSTOLLER, TRUSTEE,

Petitioner,

v.

CWCAPITAL LLC,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

BRIEF IN OPPOSITION

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QUESTION PRESENTED

Whether this Court should revisit the Court of Appeal's unanimous decision affirming the summary judgment dismissal of a Bankruptcy Trustee's breach of contract claims in which the Trustee sought to preclude a government-approved mortgage lender from enforcing the terms of a mortgage loan insured under the National Housing Act based upon a purported unwritten modification of the loan documents where:

a) there is no conflict among the Circuits regarding the fact that loans insured by the Secretary of the Department of Housing and Urban Development under the National Housing Act cannot be modified orally or through theories of estoppel or waiver; and

b) the Court of Appeals specifically considered state law as well as federal law and determined that such a mortgage loan cannot be modified orally or through theories of estoppel or waiver under either federal or state law.

PARTIES TO THE PROCEEDING

Ann Mostoller, Trustee is the bankruptcy trustee (the "Trustee") with respect to the estate of West Pointe Properties, LP ("West Pointe"). CWCapital LLC ("CW") is a mortgage lender approved by the United States Department of Housing and Urban Development ("HUD") to originate and service loans insured by and administered through HUD. CW is not owned or controlled by any publicly traded corporation. HUD was a co-defendant in this action before the District Court. However, the Trustee sought only to appeal the grant of summary judgment to the Sixth Circuit with respect to CW, not HUD. CW, as mortgage lender, noticed the borrower's default at the request of HUD and subsequently assigned the loan to HUD at HUD's direction. HUD, not CW, ultimately foreclosed upon the mortgaged property.

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STATUTORY PROVISIONS INVOLVED

This matter involves a dispute over the enforcement of the terms of a mortgage loan federally insured by the United States Department of Housing and Urban Development pursuant to the National Housing Act, 12 U.S.C. § 1701 *et seq.* (2001). In particular, section 1715z-4 governs the modification of mortgage documents covering multifamily housing. It states in pertinent part that:

> The Secretary shall not consent to any request for curing a default under any mortgage covering multifamily housing . . . or for a modification of the terms of such mortgage, except in conformity with regulations prescribed by the Secretary in accordance with the provisions of this section.

12 U.S.C. § 1715z-4 (2001).

STATEMENT OF THE CASE

The Trustee sets forth an extensive factual recitation in her Petition for Writ of Certiorari (the "Petition") based upon her contention that there "was reliance on factual errors by the lower courts in their opinions." [Petition at 3]. While the Court rarely grants certiorari "when the asserted error consists of erroneous factual findings," U.S. Sup. Ct. R. 10, and since the Trustee's recitation of the "facts" is not supported by the record below, CW will provide the facts as resolved by the lower courts which are amply reflected in the record below.

HUD has various programs through which it promotes the creation of affordable housing by facilitating the construction or substantial rehabilitation of multifamily housing communities such as apartments and manufactured home parks. National Housing Act ("NHA"), 12 U.S.C.

§ 1701 *et seq.* (2001). It does so by, among other things, insuring HUD-approved lenders against loss on mortgage defaults. *Id.* One such program, commonly known as the Section 207 Program, encourages the construction or rehabilitation of manufactured home parks through such HUD-insured loans. 12 U.S.C. § 1713 (2001) (the "Section 207 Program"). Although HUD is not the original lender on loans made under the Section 207 Program, HUD bears the economic risk of loss should a borrower default on its loan. Because the ultimate risk of these loans is borne by the government, HUD-approved lenders (i.e. lenders approved and licensed by HUD to enter into loan agreements with respect to such loans) must strictly comply with rigid statutory, regulatory and contractual obligations in connection with the handling of these loans.

If a default (monetary or non-monetary) occurs under a mortgage loan insured by HUD under the Section 207 Program, the lender is obligated to (i) assign the defaulted loan to HUD in exchange for mortgage insurance benefits or (ii) foreclose upon (or otherwise acquire title to) the mortgaged property and convey it to HUD in exchange for mortgage insurance benefits. 24 C.F.R. § 207.258 (2004). The lender's economic risk of loss is limited to an assignment fee equal to 1.0% of the outstanding loan amount (if the lender elects to assign the defaulted loan to HUD) and the loss of one month's interest on the loan. HUD's regulations, rules and requirements, therefore, give HUD broad controls and authority with respect to the underwriting and administration of loans insured by it. 24 C.F.R. § 200 *et seq.* (2004). In fact, HUD has the sole final discretion on such loans with respect to the terms of the loan agreements, any modifications of the loan documents, any extensions of any deadlines imposed under the loan documents, any advances of monies under the loan documents and any changes to the building plans and specifications. *Id.* The HUD-approved lender must comply with any determinations of HUD.

In 1996, West Pointe obtained a HUD-insured loan through Continental Wingate Associates, Inc., CW's predecessor, in the amount of $2,222,900.00 pursuant to the Section 207 Program, for the purposes of developing and constructing a mobile home park to be known as the West Pointe Community Mobile Home Park (the "Project"), in Knoxville, Tennessee (the "HUD-Insured Loan"). Petitioner's Appendix ("Pet'r App.") at A-16.[1] In connection with the HUD-Insured Loan, West Pointe executed a Deed Of Trust Note ("Note"), a Deed of Trust ("Deed of Trust"), a Security Agreement ("Security Agreement"), a Building Loan Agreement ("Building Loan Agreement"), a Regulatory Agreement ("Regulatory Agreement") and various other HUD-form documents required by HUD as a condition of insuring the HUD-Insured Loan (collectively, the "Loan Documents").[2] *Id.* Through the Loan Documents, CW, after

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[1] The District Court opinion below in *Mostoller v. HUD*, No. 3:02-CV-291 (E.D. Tenn. Jul. 18, 2003) granting CW and HUD's motions for summary judgment and dismissing the action is reproduced in the Petitioner's Appendix at A-15 through A-31.

[2] Another document executed by West Pointe at the closing of the HUD-insured Loan was a Remarketing and Extension Agreement which the Trustee disingenuously characterizes as an "Extension Agreement." [Petition at 6-7]. Before the Sixth Circuit, the Trustee claimed for the first time (as it misleads this Court in the Petition) that the Remarketing and Extension Agreement "sets forth the terms of continued construction" if "CW elects not to terminate the loan." [*Id.*]. However, as correctly emphasized by the Sixth Circuit, this agreement

> specifically **disclaims** any modifications of the deadline or any other requirement in the loan agreement: [by stating] . . . Lender's right to receive fees for extending the date of Final Endorsement shall not be construed to give [West Pointe] the right to any extension . . . [West Pointe] acknowledges that [CW] is not

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permission and authorization from HUD, agreed to make advances of loan proceeds to West Pointe to fund the construction of the Project. *Id.* The Note obligated West Pointe to repay the HUD-Insured Loan pursuant to a fixed schedule with interest only due for the first eleven months and principal and interest due each month thereafter. *Id.* The Note was secured by the Deed of Trust, which placed a first lien on the Project and provided various remedies in the event of a default. The Deed of Trust provided that a default under either the Building Loan Agreement or the Regulatory Agreement constituted a default under the Deed of Trust. *Id.*

Pursuant to the Building Loan Agreement, West Pointe was required to complete construction of the Project by July 7, 1997, eleven months after the closing of the HUD-Insured Loan. *Id.* at A-17. The Construction Contract that West Pointe signed with its general contractor, J. Hicks Excavating, Inc., however, provided for a shorter construction period to ensure that West Pointe's obligations under the Loan Documents could be fulfilled. *Id.* Both the Building Loan Agreement and the Construction Contract provided that any changes therein had to be approved in writing by CW and HUD. *Id.* In addition, the Construction Contract provided that "[t]he time by which the work shall be completed may be extended in accordance with the terms of said AIA General Conditions only with the prior written approval of the Commissioner [HUD]." *Id.* West Pointe acknowledged in the Building Loan Agreement that failure to complete the Project by July 7, 1997 or cessation of work on the Project for a period of more than 20 days (among other things) constituted defaults. *Id.* In addition, the Deed of Trust and the Security Agreement,

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> obligated to grant any extensions . . . and that by granting of one or more extensions shall not obligate [CW] to grant any additional or further extensions.

Pet'r App. at A-10-11 (emphasis supplied).

through which West Pointe pledged the Project and certain other property as collateral for the HUD-Insured Loan, specifies various events of default including failure to make a payment when due and a default or breach of any of the Loan Documents. *Id.*

Upon an event of default, CW was authorized to accelerate the HUD-Insured Loan and declare a default. *Id.* The Security Agreement signed by West Pointe and CW provided that "no waiver by the Secured Party [CW] of any event of default [would] operate as a waiver of any other event of default or of the same event of default on a future occasion." *Id.* Moreover, CW, as the secured party, could "delay in exercising or omit to exercise any right or remedy . . . without waiving that or any past, present or future right or remedy." *Id.* at A-17-18. The Security Agreement also contained a prohibition against unwritten modifications in that it stated it "may not be amended, altered or changed other than in a writing signed by" CW and West Pointe and the Security Agreement and the other "Loan Documents represent the entire agreement between [CW] and [West Pointe]."[3] *Id.* Finally, at closing, West Pointe executed a Certification of Mortgagor that certified that "the terms and conditions of the loan as reflected in the Loan Documents have not been amended, modified or supplemented, directly or indirectly, by any other agreement or understanding of the parties or waiver of any of the material provisions of the Loan Documents." *Id.*

From almost the outset of the construction of the Project, problems arose with the progress of construction. *Id.* Under

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[3] Not only did the Loan Documents and HUD regulations require that all modifications be in writing, but the HUD Form 92437 entitled Request for Construction Changes on Project Mortgages (which West Pointe routinely utilized during the construction of the Project) specified that "time extension[s must be] on a separate form."

the Loan Documents, as between CW and HUD, the responsibility for inspecting the progress of completion and conformity of the construction work was vested entirely with HUD. *Id.* HUD inspection reports from an early date reflected slow and problematic construction. *Id.* In January 1997, West Pointe submitted a request for a six-month extension of the construction completion date. HUD denied in writing the request for the six-month extension and permitted only an additional 87 days for rain delays, extending the date from February 1997 until May 1997. *Id.* West Pointe failed to complete the construction within the time allotted. *Id.* On May 8, 1997, West Pointe submitted a second extension request, which was rejected by HUD in writing on July 9, 1997. *Id.* In a letter dated July 9, 1997, HUD's representative, William McClister, explained the reason for the denial of the request to extend the construction completion deadline as "unacceptable" because: "[a]dditional time to complete the work has not been justified as required by the general conditions. Also, my staff has not observed a proper, concerted effort . . . to complete this job in a timely manner." *Id.* No extension could be given without HUD's approval. *Id.*

As of July 7, 1997 – with construction only about twenty percent completed – West Pointe was in default under the Loan Documents for its failure to complete construction by the construction completion deadline set forth in the Loan Documents. The Loan Documents explicitly required written approval by HUD for the construction completion deadline to be extended. *Id.* at A-10;[4] *see also* Pet'r App. at A-17-18. It is undisputed that no such approval was granted. To make matters worse, the general contractor ceased construction and withdrew his equipment and personnel from the job in July

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[4] The Sixth Circuit's opinion in *Mostoller v. CWCapital, LLC*, 2004 FED App. 0148N (6th Cir.) is reproduced in the Petitioner's Appendix at A-1 through A-12.

and then again, permanently, in October 1997 following disputes with West Pointe. *Id.* at A-19. In December 1997, approximately ten months after the original construction completion deadline of February 1997, and seven months after the extended construction completion deadline approved by HUD, the Project was still only twenty-five to thirty percent completed and there was no hope that construction could be completed in less than another year. Indeed, West Pointe could not obtain another general contractor at that time. *Id.* at A-4, A-19.

In addition to the construction-related defaults under the Loan Documents, West Pointe failed to make payments due under the Loan Documents. *Id.* at A-5. First, West Pointe failed to pay $23,566 to keep the HUD-Insured Loan in balance pursuant to the approval of a change order requested by West Pointe and approved by HUD which was conditioned upon funding of it by West Pointe.[5] *Id.* In addition, West Pointe breached the terms of the Loan Documents by failing to make the payment of interest and escrows due on November 1, 1997. *Id.*

On November 5, 1997, HUD notified CW in writing that West Pointe "may have violated various provisions of the [Building Loan Agreement]" and directed CW's attention to the "remedies available to the lender in the case of a default by the borrower." *Id.* at A-19. In that letter, HUD listed a litany of potential improper actions taken by West Pointe including concerns that the borrower was also impermissibly functioning as the general contractor, that Mr. Ronald Frye (West Pointe's former principal) had improperly removed the general contractor from the Project, that the borrower

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[5] Failure to keep the HUD-Insured Loan in balance (i.e. to provide funds in excess of unadvanced loan proceeds needed to complete the Project) constituted another default under the Building Loan Agreement.

apparently had failed to deposit the amount of $23,566 as required by a fourth Change Order and that HUD procedures precluded additional advances when this occurs. *Id.* at A-5. HUD made it clear to CW that no further advances of loan proceeds would be approved and that CW had to declare a default and assign the HUD-Insured Loan to HUD or exercise one of its other options for defaulted loans or lose the right to its mortgage insurance benefits. *Id.* at A-19.

As a result of the monetary and other numerous defaults under the Loan Documents, on December 10, 1997, acting upon HUD's recommendation, CW declared the HUD-Insured Loan in default and exercised its right pursuant to the Loan Documents to accelerate the HUD-Insured Loan. *Id.* Indeed, CW did not have any discretion with respect to the decision to declare the default as CW was required, pursuant to HUD regulations, to declare the default at that time.[6] Thereafter, CW assigned the HUD-Insured Loan to HUD in accordance with HUD regulations.[7] *Id.*

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[6] HUD regulations clearly define what constitutes a default. 24 C.F.R. § 207.255. Defaults are defined as "failure of the mortgagor to make **any** payment due under the mortgage" and "failure to perform **any** of the covenants under the provisions of the mortgage." 24 C.F.R. § 207.255(a)(1-2) (emphasis supplied). CW was required to notify the Commissioner in writing of such default "within 30 days." 24 C.F.R. § 207.256(a). An uncured default, which continues for a period of 30 days, triggers a mortgagee's entitlement to insurance benefits. 24 C.F.R. § 207.255(c). A mortgagee's failure to provide the notice of default within the required time limitations could result in a loss of the insurance benefits under the Section 207 Program.

[7] CW had sought permission from HUD for an extension of time to assign the HUD-Insured Loan; but **HUD denied** that request. It was within HUD's sole discretion whether to permit additional time for the election to assign. 24 C.F.R. § 207.258(b). Thereafter, CW did not have discretion as to how to handle the defaulted HUD-Insured Loan. It was required either to assign the HUD-Insured Loan to HUD or to acquire and convey title to the Project through foreclosure or other proceedings. 24 C.F.R. § 207.258.

After CW assigned the HUD-Insured Loan to HUD, all rights and duties of CW with respect to the HUD-Insured Loan were transferred from CW to HUD. *Id.* CW received no economic or other benefit from the declaration of default and the assignment.[8] Thereafter, while CW was no longer involved in any manner with the HUD-Insured Loan or the Project, West Pointe had an additional year an a half to cure the defaults or reach a work-out agreement with HUD in order to prevent foreclosure. *Id.* at A-5-6, A-19-20. HUD notified West Pointe on February 18, 1997 that CW had assigned the mortgage and invited West Pointe to cure the default. *Id.* at A-19. Over a month later, HUD notified West Pointe that the funds necessary to avoid foreclosure had not been received and provided West Pointe with an opportunity to show reasons why foreclosure should not take place. *Id.*

In response, West Pointe submitted an extensive memorandum to HUD in which it blamed HUD for the default and for CW's declaration of that default, stating that HUD directed CW to declare the loan in default, accelerate the balance and assign the Loan to HUD by virtue of its letter to CW dated November 5, 1997. Despite West Pointe's contentions that HUD (not CW) acted improperly in declaring the default, West Pointe had ample opportunity not only to cure the default, but also to establish, through the administrative proceedings conducted on May 14, 1998 afforded West Pointe by HUD, that the default did not exist or that foreclosure should not go through for some other reason. *Id.* at A-20. However, West Pointe failed to prove either. Rather, after a full hearing on these issues, apparently unconvinced, on November 9, 1998, HUD notified West

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[8] Rather, pursuant to HUD regulations, CW incurred a loss as it received insurance benefits that amounted to less than the full amount of the outstanding principal balance on the HUD-Insured Loan and HUD became the lender of record under the Loan Documents to pursue either a work-out with West Pointe or foreclosure.

Pointe that, pursuant to its discretion, the agency had considered all of the materials and allegations advanced by West Pointe regarding not proceeding with foreclosure and had concluded that West Pointe had "presented no legal reasons to alter HUD's decision to foreclose." *Id.* HUD held the HUD-Insured Loan for nearly a year and a half before publishing a foreclosure notice with the sale scheduled for May 27, 1999. *Id.*

West Pointe filed bankruptcy in order to stay the foreclosure by HUD. *Id.* The bankruptcy court granted HUD's motion for relief from the automatic stay and permitted HUD to foreclose on the Project. *Id.* In granting relief from the stay, the bankruptcy court stated that it was "undisputed that the Debtor (West Pointe) had made no principal payments on the August 7, 1996 Deed of Trust Note since its inception; that the Debtor had no income; . . . and that the Debtor last performed work on the property in late October 1997." *Id.* On April 27, 2000, HUD foreclosed on West Pointe's mortgage. HUD sold the Project to the highest bidder at a price of $350,000. *Id.*

The Complaint against CW and HUD was brought by West Pointe as debtor in possession[9] and asserted claims for damages under a breach of contract claim as a result of the foreclosure by HUD. *Id.* Originally, West Pointe asserted that CW should not have declared the HUD-Insured Loan in default, contending that the Building Loan Agreement was modified by oral representations providing for an "indefinite" extension of the construction deadline. *Id.* In the alternative, West Pointe asserted that a letter from HUD dated July 9, 1997 extended the completion date for the Project and that CW and HUD breached that agreement by foreclosing. *Id.*

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[9] The bankruptcy action was later converted to Chapter 7 and the Trustee continued this case under her name on behalf of West Pointe's estate.

After the lower court granted summary judgment to both CW and HUD, the Trustee appealed as to CW only, abandoning her claims that the July 9th letter extended the completion date and abandoning her argument that there was an oral modification of the loan documents. *Id.* at A-9 n.2. Instead, the Trustee claimed that CW was barred from enforcing the terms of the Loan Documents by virtue of theories of estoppel and waiver. The Trustee abandoned her claims against the government recognizing that these theories cannot be invoked against the government. *Id.* at A-8 n.1. Yet, she pursues these theories against CW – a HUD-approved lender acting at HUD's direction – for damages purportedly caused by HUD's foreclosure of the Project.

THE DECISIONS BELOW

Before the District Court, the Trustee argued that CW should not have declared a default because the Loan Documents were modified and the construction completion deadline was extended by oral representations (Pet'r App. at A-24) or by the July 9, 1997 letter. *Id.* at A-26. The District Court fully and carefully considered the full record and concluded that West Pointe was in default and that CW properly declared the loan in default and assigned the loan to HUD. *Id.* at A-29. The District Court held that the Loan Documents could not be modified by an oral representation, but rather that any modifications had to be in writing and approved by the Commissioner of HUD. *Id.* at A-24. The District Court also held that the July 9, 1997 letter was not an amendment to the Loan Documents because it was not a valid modification. *Id.* at A-28. Finally, the District Court held that CW never waived its right to declare a default. *Id.* at A-29.

On appeal to the Sixth Circuit, the Trustee abandoned her theory that the Loan Documents were orally modified and instead argued that CW somehow forfeited its rights to

declare the loan in default, relying on theories of estoppel or waiver. *Id.* at A-8-9. The Sixth Circuit unanimously rejected the Trustee's arguments, holding that "common law doctrines of waiver and estoppel cannot modify the terms of a HUD-guaranteed loan," and noting that this result would be the same under Tennessee common law. *Id.* at A-11. Indeed, the Sixth Circuit found that West Pointe was unable to establish that the July 9, 1997 letter or any conduct of CW could form the basis of a waiver or estoppel claim. *Id.* at A-11-12. The Sixth Circuit stressed that the plain terms of the Loan Documents applied and that CW was fully within its rights to declare West Pointe in default. *Id.* at A-12.

REASONS FOR DENYING THE PETITION

A. Standard of Review.

Generally, the Court "will decline to consider questions presented in a petition for certiorari that have not been considered by the lower court." *Patrick v. Burget*, 486 U.S. 94, 99 n.5 (1988); *see also, e.g., Nat'l Collegiate Athletic Ass'n v. Smith*, 525 U.S. 459, 470 (1999) ("[W]e do not decide in the first instance issues not decided below."); *J. Truett Payne Co. v. Chrysler Motor Corp.*, 451 U.S. 557, 568 (1981) ("We do not ordinarily address for the first time in this Court an issue which the Court of Appeals has not addressed.").

In addition, the Court generally only grants certiorari "for compelling reasons," where either there is a circuit split on the issue or where there is an important federal question at issue. U.S. Sup. Ct. R. 10; *see, e.g. Bunting v. Mellen*, 124 S. Ct. 1750, 1752 (2004) ("The second reason justifying a denial of certiorari is the absence of a direct conflict among the Circuits."); *Comm'r v. Estate of Bosch*, 387 U.S. 456, 457 (1967) (granting certiorari to resolve a "widespread

conflict" among the Circuits); *Rice v. Sioux City Mem'l Park Cemetery*, 349 U.S. 70, 79 (1955) (stating the importance of consistency in not granting certiorari "except in cases involving principles the settlement of which is of importance to the public, as distinguished from that of the parties, and in cases where there is a real and embarrassing conflict of opinion and authority between the Circuit Courts of Appeals"). Finally, the Court rarely grants certiorari "when the asserted error consists of erroneous factual findings or the misapplication of a properly stated rule of law." U.S. Sup. Ct. R. 10.

In this case, the Petition presents questions that were not raised or considered in any of the courts below. None of the questions presented involve a split in the Circuits or an important federal question. Finally, the Petition bases its request for certiorari on purportedly erroneous factual findings in the court below. For these reasons, the Petition should be denied and certiorari should not be granted.

B. Federal Law Governs This Dispute by Virtue of HUD's Participation as Loan Insurer and There is No Split in the Circuits to the Contrary.

The Trustee's basic contention in this litigation is that the terms of the Loan Documents governing the debtor's HUD-Insured Loan could not be enforced based upon various vague "equitable-type" claims. The Trustee apparently concedes that these equitable-type remedies are unavailable under federal law but disputes the applicability of federal law to the HUD-Insured Loan based upon her decision to pursue her appeals against the private HUD-approved lender alone.

The National Housing Act, 12 U.S.C. § 1715z-4, governs the requirements for the cure of defaults under, and the modification of, mortgage documents covering multifamily housing. It states in pertinent part that:

> The Secretary shall not consent to any request for curing a default under any mortgage covering multifamily housing . . . or for a modification of the terms of such mortgage, except in conformity with regulations prescribed by the Secretary in accordance with the provisions of this section.

12 U.S.C. § 1715z-4.

Indeed, every Circuit interpreting purported modifications to HUD-insured loans has held that federal law governs the interpretation of a HUD-insured loan and the rights and liabilities of the parties under such a loan. *VS Ltd. P'Ship v. HUD*, 235 F.3d 1109, 1113 (8th Cir. 2000) (specifically applying federal law – the National Housing Act and HUD regulations – in concluding that HUD loan documents can only be modified by a signed writing); *United States v. Victory Highway Vill., Inc.*, 662 F.2d 488, 497 (8th Cir. 1981) ("federal law, not [state] law, governs the rights and liabilities available upon default of a federally held or insured loan"); *United States v. Scholnick*, 505 F.2d 160, 164 (6th Cir. 1979) ("an overriding federal interest in protecting the funds of the United States and in securing the federal investments predominates over state interests."); *United States v. View Crest Garden Apts.*, 268 F.2d 380, 383 (9th Cir.) ("Local rules limiting the effectiveness of the remedies available to the United States for breach of a federal duty can not be adopted."), *cert. denied* 361 U.S. 884 (1959); *see also Bayvue Apts. Joint Venture v. Ocwen Fed. Bank FSB*, 971 F. Supp. 129, 131 (D.D.C. 1997) (district court applying federal law); *Teitelbaum v. HUD*, 953 F. Supp. 326, 331 (D. Nev. 1996) (district court applying federal law).

The Trustee argues, relying upon three unrelated cases not raised in her briefs below, *United States v. Kimbell Foods, Inc.*, 440 U.S. 715 (1979),[10] *Parker v. USDA*, 879 F.2d 1362 (6th Cir. 1989)[11] and *Pankow Constr. Co. v. Advance Mortgage Corp.*, 618 F.2d 611 (9th Cir. 1980),[12] that even if

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[10] In *Kimbell Foods*, the Court considered whether a uniform federal rule was needed to determine the priority of Farmers Home Administration and Small Business Association liens (pursuant to their respective loan programs) with respect to private liens. The Court held that there were intricate, well-established state laws of general applicability which obviated the need to fashion a uniform federal rule. Unlike the situation presented in *Kimbell*, in this case a clear federal rule barring unwritten modifications to HUD-insured loan documents and a clear federal regulatory scheme – embodied at 24 C.F.R. § 207.256b and 24 C.F.R. § 221.761(a)(2) – already exist under which to resolve the dispute at issue in the present action. Furthermore, the ruling in *Kimbell Foods* spoke to the regulation of private and consensual lien priorities and is neither dispositive nor reflective in any way of the transaction at issue in the present action.

[11] The Trustee inappropriately seeks to extend the dicta of *Parker* from the context of the Farmers Home Administration ("FmHA") loan program to HUD's Section 207 insured loan program. Such a leap is misguided, as the guidelines of the FmHA program are markedly distinct and, indeed, less stringent, than those of the HUD Section 207 loan program. Indeed, the dicta from *Parker* regarding the relationship between the FmHA, the lender and the borrower has little, if anything to do with the relationship between HUD, CW and West Pointe and even less to do with the application, in this case, of federal law. The *Parker* case does not even address the issue of the applicability of federal law. Moreover, it is clear that the *Parker* case does not support the argument that there is a conflict among the Circuits with respect to the issues raised in this case since *Parker* (like the decision below) is a Sixth Circuit case.

[12] The Trustee erroneously seeks to analogize the issue at bar to *Pankow*, in which the court found the application of California state law appropriate in resolving a dispute between a general

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federal law prohibits the enforcement of non-written modifications of loans against the government, this is not the case with respect to private lenders. However, no such distinction exists. These three cases do not support the Trustee's analysis of the specific type of HUD-sponsored lending relationship at issue here. Indeed, these cases are factually very different and their legal holdings do not support the Trustee's contentions. In fact, since HUD steps into the shoes of the HUD-insured lender when a defaulted HUD-insured loan is assigned to HUD, it would be prejudicial to the government to allow a private lender to waive rights under the loan documents without HUD's approval or to estop the government from enforcing the loan documents.

Moreover, cases with similar facts have all concluded that the prohibition against non-written modifications to HUD-insured loans applies with equal force whether the government or a private lender is involved. *Bayvue Apts. Joint Venture v. Ocwen Fed. Bank FSB*, 971 F. Supp. 129, 131 (D.D.C. 1997) (in stating that "since [private bank] was never a party to the alleged *de facto* modification agreement, the question of redressability turns on whether the alleged *de facto* agreement is or ever was enforceable," the court did

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contractor and a mortgage borrower who had secured funding under the National Housing Act. The dispute involved a private construction contract, rather than a loan document governed by HUD regulations and neither HUD nor the lender was a party to the dispute. In light of the fact that the present dispute is between the borrower and HUD-approved lender, and is wholly governed by federal regulations – any inference made by the Trustee that the holding in *Pankow* is applicable to the present action is wholly inappropriate. Additionally, the Trustee, in seeking to establish state law as the governing standard for the present action, completely ignores the Sixth Circuit's finding that "West Pointe's waiver and estoppel claims are baseless even if we apply Tennessee common law." Pet'r App. at A-11. The Ninth Circuit's ruling in *Pankow* is in no way "on point" with the current dispute and is certainly not dispositive of the issue in this case.

not distinguish between enforceability of the loan modification against the private lender or the government); *Multifamily Mortgage Trust 1996-1 v. Century Oaks Ltd.*, 532 S.E.2d 578, 582 (N.C. Ct. App. 2000) (upholding summary judgment for lender on borrower's claims that terms of loan documents were waived by a provisional work out agreement); *see also Victory Highway Vill., Inc.*, 662 F.2d at 497 (in stating that "federal law, not [state] law, governs the rights and liabilities available upon default of a federally held or insured loan," the court made no distinction between whether enforcement was against the government or the private lender).

The court in *Victory Highway* emphasized the importance of the enforcement of the terms of federally insured mortgages explaining:

> It is essential to the confidence of public and private lenders that the clear written terms of mortgages be implemented and enforced by the courts. Without such enforcement, **extrinsic judicial doctrines that frustrate the terms of the mortgage documents, and any subsequent 'work-out' arrangements, will impair the confidence of public and private lenders.** Through strict enforcement of the terms of the mortgages and recognition of HUD's right to foreclose on default, "the federal policy to protect the treasury and to promote the security of federal investment which in turn promotes the prime purpose of the Act to facilitate the building of homes by the use of federal credit will be preserved."

Victory Highway, 662 F.2d at 495 (emphasis supplied). The court explicitly rejected any type of waiver or estoppel argument which contradicted the terms of the written loan documents despite a written provisional month-to-month

work out arrangement. Indeed, the court made clear that the delay in exercising the right to pursue foreclosure does not indicate a waiver of the right to foreclose nor does it constitute an indefinite extension of the borrower's right to cure a default as advocated by the Trustee here. Once again, the application of such theories as waiver or estoppel to CW would have the effect of a waiver or estoppel of HUD's rights as CW's assignee of the loan. In such instances, the government, not CW, would incur the loss.

Not only is the Trustee's theory of recovery barred by the law, but there is nothing in the record to support such a waiver claim. Indeed, as indicated by the trial court, the undisputed facts indicate that CW did not have the authority and discretion to "waive" any rights under the Loan Documents, did not relinquish the right to declare the HUD-Insured Loan in default and made no indications to the contrary. Pet'r App. at A-28-29. The Trustee concedes that there has been no written expression of waiver. The Trustee does not assert any consideration for her waiver theory. And, at the time when CW (at the recommendation of HUD) declared the HUD-Insured Loan in default and assigned it to HUD, there was no possibility of West Pointe curing the defaults in the near future. To judicially create an indefinite extension of the construction completion deadline imposed by the Loan Documents with respect to the HUD-Insured Loan would frustrate the heart of the prohibitions against unwritten modifications and create a fraud upon the federal purse.[13] Since the waiver and estoppel theories are inapplicable to federally-insured interests and the Loan Documents cannot be modified by waiver or any other theory absent a writing expressing such modification, the trial court's

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[13] Under the Trustee's theories, a lender would have to declare a default and move to enforce its remedies immediately upon the occurrence of a default or lose forever its ability to enforce its rights. *See* Pet'r App. at A-11-12.

decision granting summary judgment and the Sixth Circuit's decision affirming the summary judgment dismissal were proper. Indeed, there is no split among the Circuits on this issue. The Sixth Circuit ruled in precisely the same manner as each of the other Circuits considering this issue.

C. The Equitable Remedies Claimed Are Unavailable and Do Not Rise to the Level of an Important Federal Issue.

As correctly concluded by the Sixth Circuit and the District Court below, the Trustee's claims that the terms of the HUD-Insured Loan Documents were modified through estoppel, waiver or some other theory is unsupported by federal law. Indeed, the various Circuits all hold that federal law precludes the modification of the Loan Documents in any manner other than through a written modification signed by all of the parties.

The National Housing Act prohibits modification of mortgage agreements through oral agreements, estoppel, waiver or other extrinsic judicial remedies. *VS Ltd. P'Ship v. HUD*, 235 F.3d 1109, 1113 (8th Cir. 2000); *Bayvue Apts. Joint Venture v. Ocwen Fed. Bank FSB*, 971 F. Supp. 129, 131 (D.D.C. 1997); *Teitelbaum v. HUD*, 953 F. Supp. 326, 331 (D. Nev. 1996). And, the applicable HUD regulations require all modifications of a mortgage agreement be made only when the parties reach such terms in writing and only with the approval of the Commissioner of HUD. 24 C.F.R. § 207.256b; *see* 24 C.F.R. § 221.761(a)(2).

For example, 24 C.F.R. § 207.256b states, in relevant part,

> The mortgagor and the mortgagee may, **with the approval of the Commissioner**, enter into an agreement which extends the time for curing a default under the mortgage or modifies the payment terms of the mortgage. The Commissioner's approval of [this] type of agreement . . . shall not be

> given unless the mortgagor agrees **in writing** that . . . it will hold in trust for disposition as directed by the Commissioner all rents or other funds derived from the property which are not required to meet actual and necessary expenses arising in connection with the operation of such property, including amortization charges under the mortgage.

(emphasis supplied). Similarly, 24 C.F.R. § 221.761(a)(2) states, in relevant part:

> In a case where the mortgage is in default, the mortgagor and the mortgagee may enter into a forbearance agreement . . . if . . . [t]he Commissioner determines that the default was due to circumstances beyond the mortgagor's control and that the mortgage probably will be restored to good standing within a reasonable period of time **and evidences such determination by written approval of the forbearance agreement**.

(emphasis supplied).

The Trustee misleadingly relies on several cases never referenced below for her theory that extrinsic judicial doctrines such as estoppel and waiver are applicable here. The Trustee's citation of *Heckler v. Cmty. Health Servs. of Crawford County, Inc.*, 467 U.S. 51 (1984) for the proposition, stated in dicta, that estoppel may lie against the government under certain circumstances is a red herring.[14]

[14] The Trustee also cites *Unites States v. Fox Lake State Bank*, 366 F.2d 962 (7th Cir. 1966), *Resolution Trust Corp. v. Vanderweele*, 833 F.Supp. 1383 (N.D. Ind. 1993) and *In re Lane*, 96 B.R. 164 (Bankr. C.D. Ill. 1988) for this proposition. These cases are inapposite. The *Fox Lake* court, ruling in a case where the government was bringing suit against a bank under the Civil False Claims Act, held that "[u]nder the peculiar circumstances of this particular case," (Cont'd)

Indeed, the Court has noted that it has reversed almost every finding of equitable estoppel on a government contract. *Office of Personnel Mgmt. v. Richmond*, 496 U.S. 414, 422 (1990).

In *Heckler*, the Court analyzed whether the government could be estopped from recovering funds erroneously paid to a medical care provider under the Medicare program, and concluded that it could not (i.e., that estoppel did *not* lie against the government). The medical care provider submitted cost reports (which were governed by regulation) which erroneously listed certain costs but which the government nevertheless paid because the regulations allowed for retroactive adjustments when the cost reports were periodically audited, should improper payments be made. Before submitting the cost reports, the medical care provider requested and received oral verification from the government's agent that the cost reports were, in fact, proper. However, when the government discovered the improperly paid costs, it sought to recover the money that was paid. The medical care provider attempted to assert that the government was estopped from recovering the money based upon the government's agent's oral verification. The Court held that estoppel was not proper because the regulations put the medical care provider on notice of the costs that were

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(Cont'd)

the government was estopped from bringing a lawsuit against the bank. Similarly, in *Resolution Trust Corp.* the court held that an estoppel affirmative defense in a lawsuit brought by Resolution Trust, a government agency, could survive a motion to strike by Resolution Trust, to the extent the estoppel affirmative defense was premised on some affirmative misconduct by the government. And, in *In re Lane*, the court noted that a government agency could not treat a contract as rejected after treating it as valid and after receiving the full benefit of the contract. None of these cases involved written loan documents or support a finding of estoppel in this case, where the government is not bringing suit, has not benefited and there is no claim of fraud or affirmative misconduct.

proper and because its reliance on an oral verification of policy by the government's agent was not reasonable.

In this case, as in *Heckler*, estoppel would not be proper. Here, West Pointe was on notice of the provisions of the Loan Documents and HUD regulations, which prohibit oral modifications of the loan documents and which state that only the Commissioner of HUD can authorize such modifications. In addition, the Trustee seeks not to estop the government based only upon a regulation, but also based upon a written loan document, which West Pointe signed. Thus, estoppel would not be proper because West Pointe had complete knowledge that the Loan Documents could only be modified with approval by the Commissioner.

In seeking to establish a basis for her claim of waiver, the Trustee once again seeks to create a dispute among the Circuits where there is none, this time erroneously analogizing the present action to the dispute at issue in *Spring Constr. Co. v. Harris*, 562 F.2d 933 (4th Cir. 1977). In *Spring Construction*, the court granted the plaintiff, a general contractor, relief against HUD for a ten percent retainage due from mortgage proceeds, holding that HUD had waived the defense of non-performance by continuing to encourage construction despite having knowledge of existing problems with the project. For many of the same reasons that the Trustee's reliance on *Pankow* as dispositive to the present action is incorrect, so too is the Trustee's reliance on *Spring Construction*.

The relationship from which the present dispute arises is between mortgage lender and borrower, a markedly different relationship than that of general contractor and mortgage lender, and indeed governed by different principles of legal responsibility and obligation. Furthermore, there is no evidence of HUD or CW "encouraging" West Pointe to

continue work on the Project such as to make claims of waiver relevant. Indeed, both the District Court and the Sixth Circuit found that the July 9, 1997 letter that the Trustee argues directs the parties to extend the contractual deadline indefinitely, "**plainly does the opposite**." Pet'r App. at A-10 (emphasis supplied).

Perhaps more important than this distinction, however, is the fact that the present action deals **specifically** with the alleged modification of HUD-insured loan agreements, while *Spring Construction* and other authorities relied upon by the Trustee[15] speak nothing to the modification of the rigidly governed terms of these HUD-prescribed loan instruments. Indeed, in *Spring Construction*, there was **no** modification of the terms of the building loan agreement or any other contract to which HUD was or was not a signatory. The central thrust of *Spring Construction* was whether non-completion of the contract was a sufficient defense for withholding mortgage retainage from the general contractor

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[15] Petitioner further relies upon the Federal Claims Court's ruling in *Carabetta Enters. Inc. v. United States*, 58 Fed. Cl. 563 (2003), as support for the assertion that acquiescence by conduct is sufficient to establish modification of the terms of a HUD-insured loan. In fact, however, the court in *Carabetta* found that HUD's offer of a capital loan (as opposed to the previously offered but subsequently repealed section 241(f) equity loans) and Carabetta's acceptance of such loan "**effected modification of the contract to that extent**." *Id.* at 567 (emphasis supplied). The court in no way extended this modification to the context of the overarching loan agreements governing issues of repayment and foreclosure such as are at issue in the present dispute. Indeed, the only reason such modification was granted was because of the clear acquiescence of both parties to accept the changed terms (clearly absent in the present dispute) and the fact that the subject loans originally agreed upon by the parties had been explicitly made illegal through Congressional action. The factual underpinnings of *Carabetta* are so distinct from the present action such that the court's holding in that case is clearly not dispositive of the present dispute.

such that claims for equitable relief by the general contractor would be unwarranted. *Spring Construction* speaks nothing to the underlying issue of the present action – the viability of non-written modifications (including theories of estoppel and waiver) to a HUD-insured loan agreement – and as such is clearly not a controlling authority in any manner.

D. Even If State Law Governed This Action, As Determined by the Lower Courts, Application of Tennessee Law Would Yield the Same Results.

The Trustee bases her Petition on the ground that the lower courts erred by applying federal law, which states that the doctrines of waiver and estoppel cannot modify the terms of a HUD-insured loan because federal regulations prohibit modification of a federally insured loan except through a written agreement. Pet'r App. at A-9. The Trustee argues that state law should apply and that, under state law, the result would be different. This is not the case.

First, the lower courts did analyze and reject the Trustee's claims under state law. *Id.* at A-11. Indeed, if (against the weight of authority) state law is applied, rather than federal law, the result is still the same. As the Sixth Circuit correctly noted in its decision, "West Pointe's waiver and estoppel claims are baseless even if we apply Tennessee common law." *Id.* at A-11.

The Tennessee Statute of Frauds states:

> No action shall be brought against a lender or creditor . . . upon any promise or commitment **to alter, amend, renew, extend or otherwise modify or supplement any written promise, agreement or commitment to lend money or extend credit**, unless the promise or agreement, upon which such action shall be brought, or some

> memorandum or note thereof, **shall be in writing** and signed by the lender or creditor, or some other person lawfully authorized by such lender or creditor.

Tenn. Code Ann. § 29-2-101(b)(1) (2003) (emphasis supplied). Moreover, under Tennessee law "all contracts, including . . . notes . . . shall be prima facie evidence that the contract contains the true intention of the parties and shall be enforced." Tenn. Code Ann. § 47-50-112(a) (2003). Thus, under Tennessee law, as under federal law, modification of a loan such as the loan at issue must be in writing. *See, e.g. Decatur County Bank v. Duck*, 969 S.W.2d 393 (Tenn. App. 1997) (affirming summary judgment in favor of lender on grounds that "absent writing memorializing" "alleged fraudulent representations by Bank that it would finance [borrower's] . . . operations until completion," such oral modification was unenforceable); *Bucholz v. Tenn. Farmers Life Reassurance*, 145 S.W.3d 80 (Tenn. Ct. App. 2003) (holding that modification of an existing contract cannot occur through an "ambiguous course of dealings" between the parties from which diverse inferences might reasonably be drawn as to whether the contract was modified or not); *Rush v. Chatanooga Du Pont Emp. Credit Union*, 210 Tenn. 344 (1962) (parol evidence is not admissible to vary, alter or contradict the terms of a written instrument); *Todd v. Third Nat'l Bank*, 172 Tenn. 586 (1938) (the terms of a note cannot be varied by oral proof and no legal conclusion can be rested upon statement of a bill which would vary positions of a note).

In addition, under Tennessee law, a waiver is an intentional relinquishment of a known right. *Ky. Nat'l Ins. Co. v. Gardner*, 6 S.W.3d 493, 498 (Tenn. 1999). To establish a waiver, "there must be a clear, unequivocal and decisive act of the party showing such a purpose or acts amounting to an estoppel on its part." *Id.* at 498-99. "The law will not

presume a waiver, and the party claiming the waiver has the burden of proving it by a preponderance of the evidence." *Id.* at 499. The Sixth Circuit found that West Pointe could not establish waiver. Pet'r App. at A-11-12.

Similarly, the Sixth Circuit rejected West Pointe's estoppel argument under Tennessee law. Estoppel, like waiver, "is not favored and it is the burden of the party seeking to invoke the doctrine to prove each and every element thereof." *Buchholz*, 145 S.W.3d at 85. The Sixth Circuit found that "West Pointe cite[d] no authority to suggest there is any jurisdiction that would find waiver or estoppel. . . ." Pet'r App. at A-12.

Under state law, as under federal law, West Pointe was unable to establish waiver and/or estoppel. Thus, any allegation that the lower court erred in applying federal law is moot, and not a basis for the grant of certiorari.

CONCLUSION

The Circuits are undivided in holding that mortgages administered under the National Housing Act cannot be modified by oral agreement, waiver or estoppel. Moreover, this is not a compelling federal issue which necessitates consideration by the Court. And, while federal law applies to loans administered under the National Housing Act, the results below would not differ under state law. Indeed, the lower courts correctly concluded that under the Tennessee Statute of Frauds, the HUD-Insured Loan could not be modified in any manner other than by a writing signed by the parties. For the foregoing reasons, CWCapital LLC respectfully requests that this Court deny the Petition.

Respectfully submitted,

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